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Ontario Energy Board



IN THE MATTER OF THE
ONTARIO ENERGY BOARD ACT
AND
IN THE MATTER OF A
REFERENCE FROM THE
LIEUTENANT GOVERNOR
IN COUNCIL

PROPOSED ACQUISITION OF THE COMMON SHARES
OF THE CONSUMERS' GAS COMPANY LTD.
BY BRITISH GAS plc

E.B.R.L.G. 35
E.B.R.L.G. 35-1
E.B.R.L.G. 35-3

REPORT OF THE BOARD

Pour des renseignements en français, veuillez communiquer
avec la Commission de l'énergie de l'Ontario.

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E.B.R.L.G. 35

E.B.R.L.G. 35-1

E.B.R.L.G. 35-3

REPORT OF THE BOARD

EXECUTIVE SUMMARY

1. This Report is a result of a reference from the Lieutenant Governor in Council who requested the Ontario Energy Board to examine an application by British Gas to purchase the 83 percent of Consumers' common shares now held indirectly by the Reichmann family of Toronto. Consumers is Canada's largest natural gas distributor serving Toronto, Ottawa, part of the Golden Horseshoe and the northshore of Lake Ontario.
2. The British Gas acquisition also includes the purchase of the 17 percent of the Consumers common shares publically traded on the Toronto and Montreal stock exchanges. The total purchase price at \$34 per share is approximately \$1.1 billion.
3. The Board finds that British Gas is a financially strong company, stronger than Consumers' present owner, GW, and Consumers itself. Because the physical gas distribution system must continue to be in Ontario, and the regulatory regime will continue to function unaffected by this transaction, the Board finds that ownership of Consumers by British Gas, solely because the latter is a foreign company, would not be contrary to the public interest.
4. Equally important as the foreign control issue, in the Board's view, is the elimination of the existing public float of common shares which is expected to occur because of Ontario's securities legislation requiring British Gas to extend the same price offer to all minority shareholders in Ontario, and British Gas' intent to extend the offer to minority shareholders regardless of residency. Having carefully weighed all the evidence, the Board finds that the elimination of the public float would be contrary to the public interest and the Board therefore recommends that a plan to reinstate the public float should

be a Condition of Approval and the maintenance of such float should continue to be an undertaking.

5. The evidence at the hearing clearly indicated that, absent new legislation, undertakings are useful and accepted by most parties including Consumers' current owner and British Gas. It is the Board's opinion that if the acquisition by British Gas is approved, the undertakings which are presently in place should continue with certain amendments as set out in the Report. The Board has recommended several key amendments relating to foreign ownership which include the establishment of a treasury function within Consumers and the restriction of intercorporate financial activity between Consumers and its new affiliates limited to those incorporated and headquartered in Ontario.
6. There will be an approximate \$1.1 billion capital inflow associated with this transaction. However, there was no consensus by economists or other witnesses as to the impact of this on the domestic economy. Opinion ranged from favourable to neutral to unfavourable. The Board however senses that, if emotion is put aside, an inflow of foreign capital will, on balance, be of some benefit to the domestic economy.
7. A recurring problem in similar takeover examinations is the inherent difficulty acquiror companies have in providing detailed financial and business plans for the target companies. The Board is therefore unable to judge with confidence the expectations of British Gas' shareholders and managers regarding Consumers' performance. The Board simply notes and reports the testimony by British Gas' senior personnel that the Consumers acquisition represents a long-term investment and there are no plans to effect any material or adverse change in corporate policies, personnel, or more generally the management and operations of Consumers.



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8. With regard to the potential impact on Consumers' ratepayers, the Board notes that the regulatory regime in Ontario, including the provision of suitable undertakings, ensures that ratepayers will not be adversely affected by the transaction in any obvious or material way.
9. On the other hand, Consumers' current shareholders, including minority shareholders, are being offered a price for their shares in excess of the market price. If the transaction is not to proceed, the immediate monetary benefits to the shareholders may be foregone and their rights may be compromised.
10. A possible adverse impact to Ontario's public interest, if the transaction were completed, may arise from the potential disposition of Telesis, the oil and gas division of Consumers, depending on the outcome of a review by Investment Canada. Given the likely scenario of alternative ownership of the assets of Telesis, however, the Board does not consider this as sufficient basis for not recommending approval.
11. Based on its findings and conclusions the Board reports that, on balance, the proposed transaction is not contrary to the public interest if British Gas and its affiliates meet certain conditions prior to the formal granting of approval and agree to execute the undertakings recommended by the Board.

E.B.R.L.G. 35
E.B.R.L.G. 35-1
E.B.R.L.G. 35-3

IN THE MATTER OF Section 26 of the Ontario Energy Board Act, R.S.O. 1980, Chapter 332;

AND IN THE MATTER OF certain undertakings dated March 4, 1987 and given to the Lieutenant Governor in Council by GW Utilities Limited, 706377 Ontario Limited, HWR Holdings Inc., 685515 Ontario Inc. (now GW-CG Investments Limited) and The Consumers' Gas Company Ltd.;

AND IN THE MATTER OF an application dated March 16, 1990 filed by British Gas plc pursuant to Section 26 of the Ontario Energy Board Act for leave of the Lieutenant Governor in Council with respect to the proposed offer for all of the common shares of The Consumers' Gas Company Ltd. held by GW-CG Investments Limited and for leave of the Lieutenant Governor in Council pursuant to Article 3.1 of the 1987 Undertakings for the assumption of certain support arrangements in respect of certain securities of The Consumers' Gas Company Ltd.;

AND IN THE MATTER OF an application dated March 26, 1990 filed by GW Utilities Limited and GW-CG Investments Limited pursuant to Article 1.5 of the 1987 Undertakings for leave of the Lieutenant Governor in Council with respect to the proposed disposition by GW Utilities Limited to British Gas plc of its common shares of The Consumers' Gas Company Ltd. and for the release of GW Utilities Limited and GW-CG Investments Limited from the 1987 Undertakings;

AND IN THE MATTER OF a reference pursuant to Section 36 of the Ontario Energy Board Act from the Lieutenant Governor in Council by Order-in-Council dated April 20, 1990, to the Ontario Energy Board to examine and report on various matters relating to the proposed acquisition of all of the common shares of The Consumers' Gas Company Ltd.

BEFORE: S.J. Wychowaneć, Q.C.
Chairman and Presiding Member

O.J. Cook
Member

R.R. Perdue, Q.C.
Member

October 15, 1990

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REPORT OF THE BOARD



Ontario
Energy
Board

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de l'Énergie
de l'Ontario

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October 15, 1990

TO HIS HONOUR THE LIEUTENANT GOVERNOR IN COUNCIL:

By Order in Council OC 990/90, dated April 20, 1990 and Section 26 of the Ontario Energy Board Act, the Ontario Energy Board was directed to examine and, after holding a public hearing, to report on matters dealing with the proposed acquisition and control of The Consumers' Gas Company Ltd. by British Gas plc.

The Board herewith submits its Report and Recommendations.

Respectfully Submitted,

S.J. Wychowanec
Chairman and Presiding Member

O.J. Cook
Member

R.R. Perdue
Member

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1. INTRODUCTION

1.1 THE APPLICATIONS AND REFERENCE

1.1.1 British Gas plc ("British Gas") filed an application dated March 16, 1990 with the Ontario Energy Board ("the Board") in accordance with Section 26 of the Ontario Energy Board Act ("the Act") for leave of the Lieutenant Governor in Council ("the LGIC") with respect to a proposed offer ("the Offer") for all of the common shares of The Consumers' Gas Company Ltd. ("Consumers") held by GW-CG Investments Limited ("GW-CG"). The Offer is to be made by a wholly-owned Canadian subsidiary of British Gas pursuant to an agreement ("the Agreement") dated March 7, 1990 between British Gas and GW Utilities Limited ("GW").

1.1.2 In accordance with Article 3.1 of certain undertakings dated March 4, 1987, given by GW, 706377 Ontario Limited, HWR Holdings Inc., 685575 Ontario Inc. (now GW-CG) and Consumers to the LGIC ("the 1987 Undertakings"), British Gas also applied for approval of the proposed assumption of support arrangements in respect of certain securities of Consumers.

1.1.3 GW and GW-CG also filed an application dated March 26, 1990 with the Board, in accordance with Article 1.5 of the 1987 Undertakings, for leave of the LGIC for GW to dispose of the common shares of

Consumers. GW and GW-CG also sought release from the 1987 Undertakings.

1.1.4 The LGIC, by and with the advice of the Executive Council, issued Order-in-Council 990/90 dated April 20, 1990 ("the Reference") requiring the Board, pursuant to Section 36 of the Act, to examine, and after holding a public hearing with respect thereto, to report to the LGIC on the following matters:

1. The probable and potential impact of the proposed acquisition now and in the future,
 - on the business activities of Consumers;
 - on the gas customers and communities in Ontario served by Consumers;
 - on the Ontario residents employed by and the Ontario companies doing business with Consumers;
 - on the cost and quality of gas utility service; and
 - on the economic well-being of the Province.
2. The financial strength of the entity that will directly or indirectly control Consumers;
3. The financing of the acquisition and its impact on Consumers and rates for gas service in Ontario;
4. The maintenance of a public float;
5. The corporate policies, business and financial plans of the new controlling entity for the business and operations of Consumers in Ontario including but not limited to:
 - organization and management of Consumers;

- the financing for and capital structure of Consumers;
- affiliate transactions;
- participation by Consumers in activities not regulated by the Board;
- procurement policies; and
- research and development.

6. Any other impact on the public interest that in the Board's opinion may result from the granting of the application including the impact of acquisition of the control of a gas utility by a person or persons not ordinarily resident in Canada, and in particular, without limiting the generality of the foregoing, the impact of such acquisition on:

- the price of gas to Ontario consumers;
- the quality of service to Ontario consumers;
- the level of employment by Consumers in Ontario; and
- the use of dividends accruing to the foreign owner and whether they will flow out of Ontario or be reinvested in the Province.

1.1.5 Section 26(2) of the Act provides that:

No person, without first obtaining the leave of the Lieutenant Governor in Council, shall acquire such number of any class of shares of a gas transmitter, gas distributor or storage company that together with shares already held by such person or by such person and an associate or associates of such person will in the aggregate exceed 20 percent of the shares outstanding of that class of the gas transmitter, gas distributor or storage company.

1.1.6 Article 1.5 of the 1987 Undertakings provides, in part, that:

No action shall be taken by a shareholder or Consumers, without first obtaining leave of the Lieutenant Governor in Council, that will result in any person acquiring:

(a) more than 20 percent of the voting shares of Consumers.

Application for leave, as required above, shall be made to the Ontario Energy Board.

1.1.7 Article 3.1 of the 1987 Undertakings provides that:

Any support arrangements existing subsequent to the dissolution of Walker-Home Oil Limited and Hiram Walker Resources Ltd. whereby HWR Holdings or its affiliates have guaranteed or supported the bonds, debentures, loans or preference shares of Consumers shall not be altered without the prior approval of the Ontario Energy Board.

1.2 THE HEARING

1.2.1 On April 9, 1990 the Board issued a Notice of the British Gas Application (E.B.R.L.G. 35) and the GW, GW-CG Application (E.B.R.L.G. 35-1). Through procedural orders, the Board combined for the purpose of this hearing the above applications with the Reference (E.B.R.L.G. 35-3), abridged the time for receipt of interventions and applications for intervenor funding, set out certain dates relevant to the combined hearing, and directed that certain information be filed by the applicants prior to the hearing.

1.2.2 An application relating to a proposed amalgamation of Consumers with GW-CG (E.B.R.L.G. 35-2) was withdrawn.

1.2.3 The Notice of Hearing was issued by the Board on May 23, 1990 pursuant to which an Issues and Procedural Day was held on May 30, 1990 and the hearing of evidence commenced on June 26, 1990. The evidentiary portion of the hearing took 11 sitting days to July 11, 1990. The proceedings were completed with final reply argument being received by the Board on August 7, 1990.

1.2.4 A copy of the verbatim transcript of the proceedings and all exhibits are available for review in the Board's offices.

1.2.5 The Board has evaluated all the relevant evidence and submissions. However, it has chosen to summarize the evidence and positions of the parties only to the extent considered necessary or appropriate to deal with specific issues.

1.3 INTERVENOR FUNDING

1.3.1 On June 1, 1990 the Board heard three applications for intervenor funding pursuant to the Intervenor Funding Project Act, 1988 ("IFPA"). The parties were Energy Probe, Council of Canadians and F. Warren Hurst. The Board issued its Decision with Reasons on this matter on June 13, 1990, whereby all three applicants qualified for funding and were granted various amounts. Pursuant to Section 12 of the IFPA, Mr. Hurst requested supplemental funding which, following a hearing, was granted.

1.4 APPEARANCES

1.4.1 The following is a list of participants in the hearing and their representatives:

British Gas

J.M. Roland, Q.C.

A. Dadson

Board Staff	J.A. Campion
GW/GW-CG	S. Sharpe
Consumers	P.Y. Atkinson
Council of Canadians	D.I. Poch
Energy Probe	D. Chapman M. Mattson
F. Warren Hurst	S.T. Goudge, Q.C. M.L. Madras
The Municipality of Metropolitan Toronto	P. Fontaine
Mutual Gas Association	S. Tenenbaum
Union Gas Limited ("Union")	D.A. Sulman

1.5 **WITNESSES**

1.5.1 The following witnesses appeared on behalf of British Gas:

A. Sutcliffe	Managing Director, Group Finance, British Gas
G. Langshaw	Managing Director, Global Gas, British Gas
G. Clerehugh	Director of Technology, British Gas

J.R. Peacock	Managing Director, Morgan Guaranty Trust, J.P. Morgan Inc.
R.D. Falconer	Vice-President and Director, Wood Gundy Inc.
G.L. Reuber	Former Deputy Minister of Finance, Government of Canada
A.E. Safarian	Professor of Business Economics, Faculty of Management, University of Toronto
L. Waverman	Professor of Economics, Department of Economics, University of Toronto

1.5.2 The following Consumers employees appeared as witnesses:

R.J. Craig	General Manager, Telesis Oil and Gas Division
R.E. Potts	Executive Assistant to the President, Responsible for Strategic Planning, Research and Development
R.G. Riedl	Vice-President, Gas Supply
S.J. Szilard	Director, Technology and Development

1.5.3 The following witnesses appeared on behalf of Board Staff:

W. T. Cannon	Associate Professor of Finance, School of Business, Queen's University
T. E. Kierans	President, The C.D. Howe Institute
M. H. Watkins	Professor of Economics and Political Science, University College, University of Toronto

1.5.4 The following witnesses appeared on behalf of Council of Canadians:

M. V. Barlow National Chairperson, Council of
Canadians

M. Bradfield Professor, Department of Economics,
Dalhousie University

1.5.5 L. G. Dodd, Chief Operating Officer of O & Y Enterprises Inc.,
appeared as witness on behalf of GW and GW-CG.

1.5.6 J. O. Gibbons, Senior Economic Advisor, Canadian Institute for
Environmental Law and Policy, appeared as witness on behalf of
Energy Probe.

1.5.7 F. Warren Hurst appeared as witness on his own behalf.

1.5.8 H. Tenenbaum, President of Mutual Gas Association, appeared as
witness on behalf of Mutual Gas Association.

1.6 **LETTERS OF COMMENT**

1.6.1 The Board received written comments from the following parties:

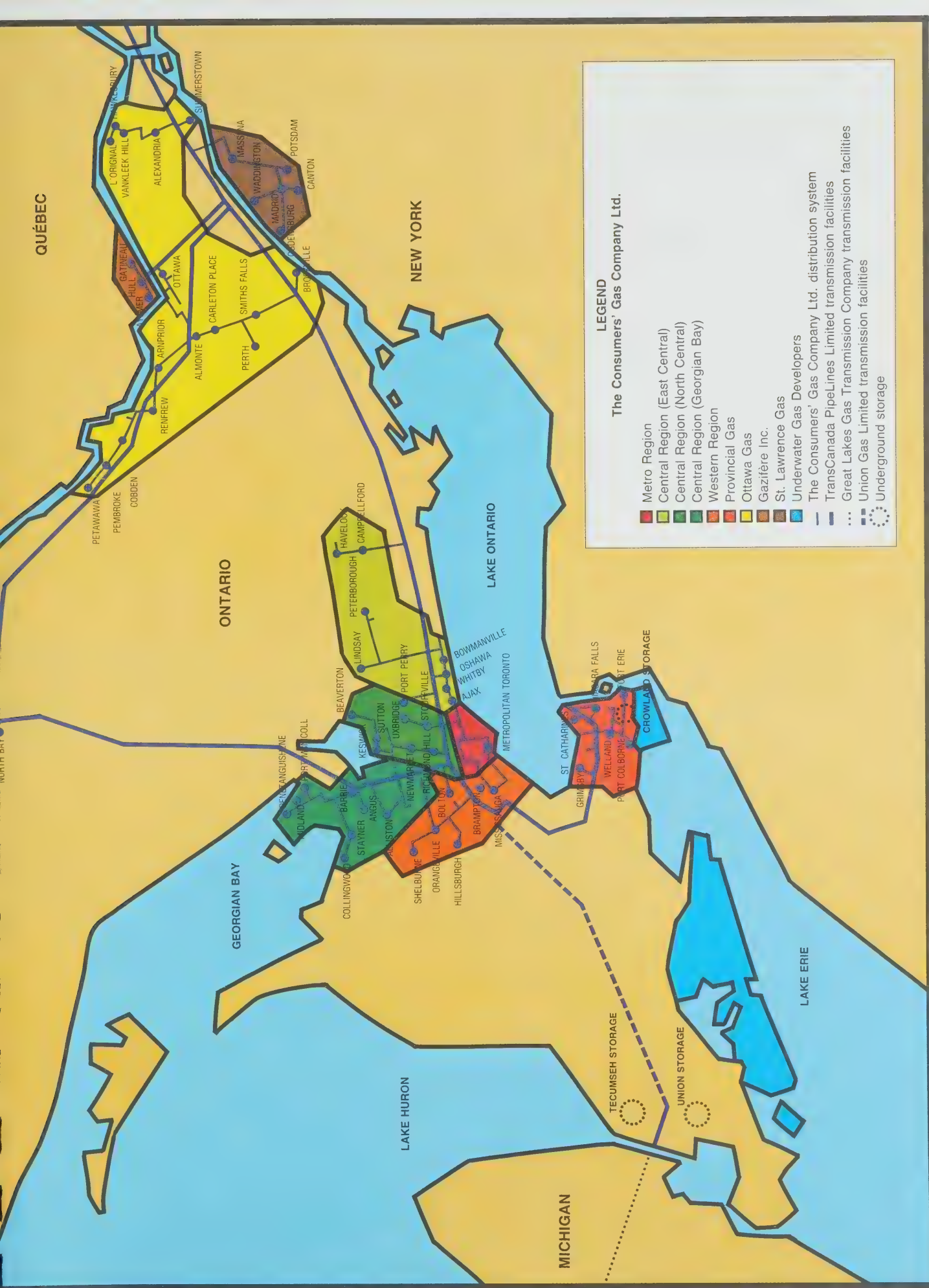
- City of Toronto
- The Municipality of Metropolitan Toronto, Parks and Property
Department
- F.T. Gerson Limited, Consulting Engineers
- J.A. Taylor.

2. THE PARTIES TO THE TRANSACTION

2.1 CONSUMERS, GW-CG AND GW

2.1.1 Consumers, with its head office in Toronto, is the largest natural gas distributor in Canada. It is subject to the Ontario Business Corporations Act, 1982. It has assets of over \$2 billion and it serves over one million residential, commercial and industrial customers in central and eastern Ontario including: Metropolitan Toronto and its vicinity, Mississauga, Ottawa, Brockville, Peterborough, Barrie, St. Catharines, Niagara Falls and many other Ontario communities. In addition, Consumers serves the areas in and around Hull, Quebec, through Gazifère Inc., and in northern New York State, through St. Lawrence Gas Company, Inc. Consumers has some 5,000 employees. A map of the Consumers distribution system is shown on the following page.

2.1.2 The utility business of Consumers in Ontario is conducted under statutes and municipal by-laws which grant it the right to operate in the areas served. The storage, transmission, distribution and sale of natural gas in Ontario are regulated by the Board. Consumers purchases gas for its Canadian utility operations from Western Gas Marketing Limited ("WGML"), a number of other suppliers, including

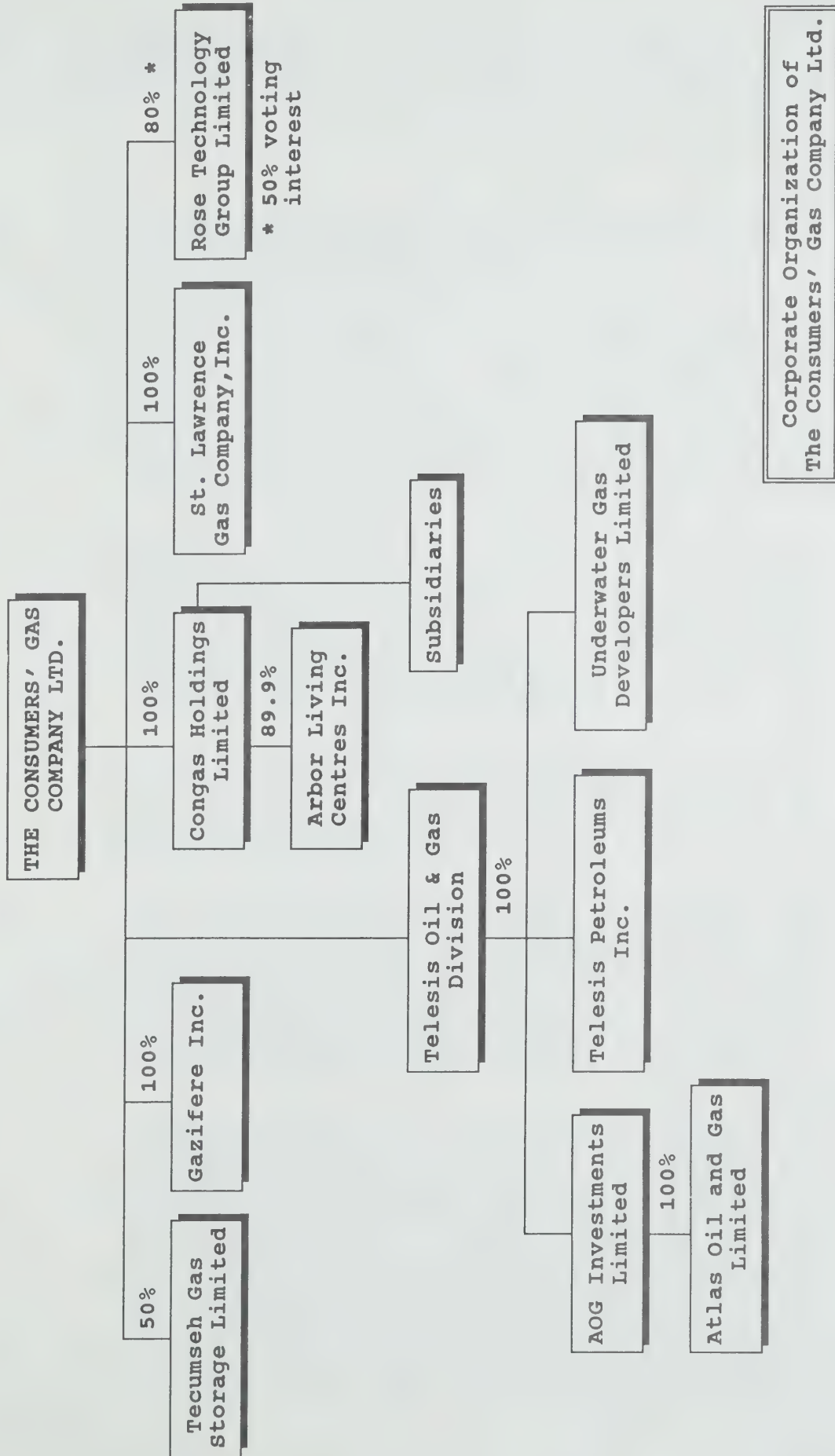


LEGEND **The Consumers' Gas Company Ltd.**

- Metro Region
- Central Region (East Central)
- Central Region (North Central)
- Central Region (Georgian Bay)
- Western Region
- Provincial Gas
- Ottawa Gas
- Gazifère Inc.
- St. Lawrence Gas
- Underwater Gas Developers
- The Consumers' Gas Company Ltd. distribution system
- TransCanada PipeLines Limited transmission facilities
- Great Lakes Gas Transmission Company transmission facilities
- Union Gas Limited transmission facilities
- Underground storage

its Telesis Oil and Gas Division ("Telesis"), its affiliates, and from a number of its customers through direct purchase arrangements.

- 2.1.3 In addition to its regulated utility operations, which include appliance merchandising, Consumers' other main activities include: energy management through Rose Technology Group Limited; the exploration for and production of oil and gas primarily in southwestern Ontario through Telesis; contract drilling for gas and oil in Ontario and the northeastern United States through Underwater Gas Developers Limited; natural gas and petroleum consulting in Canada and internationally through Congas Engineering Canada Ltd.; and nursing and retirement homes in Canada and in the United States through Arbor Living Centres Inc. ("Arbor"). In January 1990, Consumers announced its intention to sell Arbor.
- 2.1.4 Consumers also has a 50 percent equity interest in, and is the major customer of, Tecumseh Gas Storage Limited ("Tecumseh Gas"), a company operating major underground gas storage in Ontario. Imperial Oil Limited is the other owner of Tecumseh Gas.
- 2.1.5 A schematic presentation of the Consumers group of companies is shown on the following page.
- 2.1.6 At September 30, 1989, the book value of Consumers' assets was approximately \$2.1 billion. The common and preferred equity ratios were 32 percent and 6 percent respectively while the total debt ratio was 62 percent. Operating revenue for fiscal 1989 was \$1.8 billion and net income \$103 million, prior to payment of a dividend on preference shares. The income applicable to common shares was \$92 million and the return on average common equity was 15.8 percent. The consolidated balance sheet and income statement pertaining to the



Corporate Organization of
The Consumers' Gas Company Ltd.

July 1990

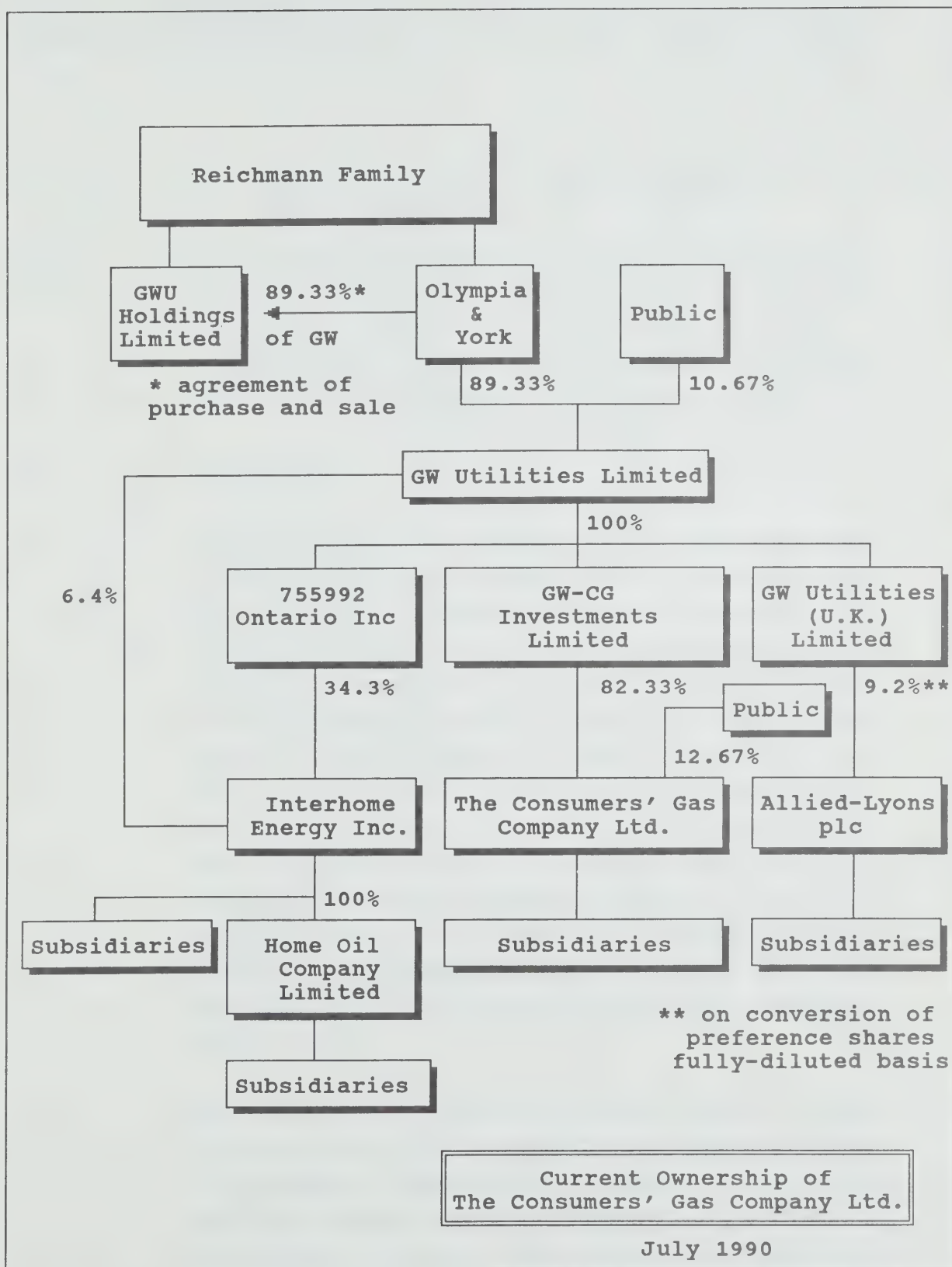
1989 fiscal year of Consumers and British Gas are shown in Tables 1 and 2 at the end of this chapter.

- 2.1.7 The majority of the assets and income of Consumers is associated with its Ontario utility operations. The Ontario utility rate base for the 1990 fiscal year was \$1.5 billion as determined by the Board in its E.B.R.O. 464 Decision. In that Decision, the Board determined an allowable rate of return on common equity of 13.25 percent.
- 2.1.8 According to information at the time of the hearing, there were approximately 3,500 registered holders of Consumers' common shares. The common shares are listed on the Toronto and Montreal Stock Exchanges. About 83 percent of the common shares are held by GW-CG which is a wholly-owned subsidiary of GW.
- 2.1.9 GW-CG has no other material assets or liabilities and its only activity since its incorporation has been the majority ownership of the Consumers common shares.
- 2.1.10 GW's indirect shareholding in Consumers stems from the 1986 acquisition of Hiram Walker Resources ("Hiram Walker") by Gulf Canada Corporation ("Gulf") and the subsequent 1987 reorganization of Gulf pursuant to which GW succeeded to Gulf's interest in the Hiram Walker assets, including the Consumers common shares.
- 2.1.11 GW is an Ontario corporation continuing from the amalgamation of GW and 706377 Ontario Inc. and later with HWR Holdings Inc. GW also owns, directly or indirectly, approximately 41 percent of the outstanding common shares of Interhome Energy Inc. and a 9.2 percent interest in Allied-Lyons plc. About 89 percent of the common shares of GW are owned by Olympia & York Developments Limited ("Olympia & York"). In January 1990, Olympia & York agreed to sell all of its common shares of GW to GWU Holdings Limited, a

private corporation, all of the shares of which are beneficially owned, directly or indirectly, by members of the Reichmann family. The present ownership of Consumers is depicted in the figure appearing on the following page.

2.1.12 Consumers' business and its relationship with its affiliates has been subject to the 1987 Undertakings, key features of which include the following:

- maintenance of a public float of voting common shares of no less than 15 percent;
- a majority of independent members of the Consumers board of directors;
- separate external auditors for Consumers and its affiliates;
- restrictions on affiliate transactions, other than gas-supply, without prior approval of the Board;
- certain support arrangements for Consumers' securities or bonds and debentures which are not to be altered without the prior approval of the Board;
- maintenance of an appropriate level of common equity for Consumers;
- restrictions on intercorporate indebtedness, guarantees and investments; and



- restrictions on Consumers' business diversification.

2.1.13 GW, the indirect owner of Consumers, provides treasury services to Consumers on a cost recovery basis. Gas supply transactions, long-term or spot, as well as certain financial transactions aimed at reducing income tax liabilities for the group of companies have taken place from time to time between Consumers and its affiliates.

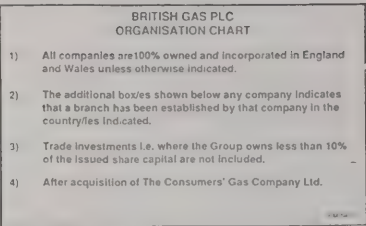
2.2 BRITISH GAS

2.2.1 British Gas is incorporated under the laws of England and Wales and is headquartered in London, England. British Gas was a state-owned corporation until it was privatized in December 1986 through a public offering conducted in the United Kingdom and in leading international markets, including Canada. The ordinary or common shares of British Gas are traded on stock exchanges in London and Tokyo, and through American Depositary Receipts, or "ADRs", on stock exchanges in New York and Toronto. The ordinary shares and ADRs are widely held. According to British Gas, no one party currently owns more than 5 percent of British Gas' outstanding ordinary shares. The Articles of Association of British Gas set an upper ownership limit of 15 percent by any one party. Through its ownership of a Special Share ("the golden share"), the British Government can veto, by withholding consent, a change in the Articles of Association relating to this provision.

2.2.2 British Gas serves approximately 18 million customers in Great Britain and, for the fiscal year ended March 31, 1989, its total assets were equivalent to approximately \$26.5 billion. (Throughout this Report, an exchange rate of £1 = \$1.96 Cdn. is used, which was the rate in effect at the time the Offer was announced. At the time of writing this Report, the exchange rate was about £1 = \$2.26 Cdn.)

- 2.2.3 Although the primary business of British Gas is the purchase, distribution and sale of gas, that business is supported by other major activities. It owns and operates a range of gas storage facilities, including six liquefied natural gas installations, seven underground salt caverns, and a depleted gas well in the North Sea. Its other major activities include a major and increasing investment in oil and gas exploration and production, a broad range of services to customers, and the marketing of gas appliances.
- 2.2.4 The involvement of British Gas in oil and gas exploration and production activities has expanded significantly since its privatization. British Gas' expansion has included the purchase in 1988, through a wholly-owned Canadian subsidiary, of approximately 51 percent of the equity, but approximately 33 percent of the voting shares, of Bow Valley Industries Ltd. ("Bow Valley"). Bow Valley is incorporated under the laws of Alberta and is an international resource company which conducts its activities primarily in Canada, the North Sea and Indonesia.
- 2.2.5 Other purchases have included Acre Oil plc, certain subsidiaries of Tenneco Inc. and a major holding in Texas Eastern North Sea Inc. British Gas' recent attempt to purchase Petrocorp, the New Zealand state-owned oil and gas company, failed at the last minute. British Gas attributed the failure to that Government's change of mind. Subsequently, Petrocorp was sold to local interests.
- 2.2.6 The organization of the British Gas group of companies is set out in the figure appearing on the following page, which also shows Consumers as a potential subsidiary.

BRITISH GAS PLC



2.2.7 According to information provided at the hearing, British Gas is organized into three business units. Those units are:

- i) Gas Supply, which covers the bulk purchase of natural gas and the transmission, distribution and marketing of natural gas in Great Britain;
- ii) Exploration and Production, for both gas and oil, on the U.K. continental shelf and in a growing number of other areas; and
- iii) Global Gas, comprising the New Business Development and Technology Transfer departments of British Gas. Upon completion of the proposed purchase, responsibility for Consumers would be within Global Gas.

2.2.8 The book value of British Gas' total consolidated assets, excluding the book value of Consumers' assets, for the fiscal year ended March 31, 1989 was approximately \$26.5 billion and the total debt ratio was only 26 percent. Income applicable to common shares for the 1989 fiscal year was approximately \$2.1 billion and return on average common equity, based on historical cost accounting, was estimated at 12.9 percent.

2.2.9 The consolidated balance sheet and income statement for the 1989 fiscal year, together with those of Consumers, are shown in Tables 1 and 2 respectively. Also shown in these tables are the pro forma consolidated totals reflecting the purchase of the Consumers common shares.

- 2.2.10 As shown in Table 3, British Gas' AAA rating according to Moody's, and Aaa rating according to Standard and Poor's bond rating services are equalled in Canada only by the ratings given to the Government of Canada, Petro-Canada, the Province of Ontario and Ontario Hydro.
- 2.2.11 As shown in Table 4, British Gas enjoys Value Lines' highest financial safety rank among the major Canadian energy related companies, including energy utilities.

TABLE 1				
CONSOLIDATED BALANCE SHEET OF CONSUMERS AND OF BRITISH GAS AND PROFORMA CONSOLIDATED BALANCE SHEET OF BRITISH GAS REFLECTING THE PURCHASE OF THE CONSUMERS COMMON SHARES				
	British Gas Cdn. \$ (000,000)	Consumers Cdn. \$ (000,000)	Adjustments Cdn. \$ (000,000)	Consolidated Totals Cdn. \$ (000,000)
"Fair Value"			523	523
Goodwill	319			319
Current Assets				
Cash	2,025	12		2,037
Short Term Investments	447	83		530
Accounts Receivable	3,118	103		3,221
Materials and Supplies	246	17		263
Gas in Storage	319	285		604
Prepaid Expenses	<u>88</u>	<u>11</u>		<u>99</u>
	<u>6,243</u>	<u>511</u>		<u>6,754</u>
Non-Current Investments		57		57
Property, Plant & Equipment	22,183	2,001		24,184
Acc. Depreciation & Depletion	<u>(2,854)</u>	<u>(507)</u>		<u>(3,361)</u>
	<u>19,329</u>	<u>1,494</u>		<u>20,823</u>
Other Assets & Deferred Charges	<u>559</u>	<u>69</u>		<u>628</u>
	<u>26,450</u>	<u>2,131</u>	<u>523</u>	<u>29,104</u>
Current Liabilities				
Other	1,137			1,137
Loans and Notes Payable	2,132	287	1,121	3,540
Accounts Payable	1,439	207		1,646
Income and Other Taxes	831	6		837
Dividends Payable		17		17
Current Portion of LTD		<u>13</u>		<u>13</u>
	<u>5,539</u>	<u>530</u>	<u>1,121</u>	<u>7,190</u>
Long Term Debt	1,970	860		2,830
Deferred Income Taxes	6,656	31		6,687
Minority Interest	623	4		627
Shareholders' Equity				
Preference Shares		108		108
Common Shares	2,087	278	(278)	2,087
Retained Earnings	<u>9,575</u>	<u>320</u>	<u>(320)</u>	<u>9,575</u>
	<u>11,662</u>	<u>706</u>	<u>(598)</u>	<u>11,770</u>
	<u>26,450</u>	<u>2,131</u>	<u>523</u>	<u>29,104</u>
Notes:	1. British Gas - Year to 31.3.89, Consumers - Year to 30.9.89			
	2. British Gas per Canadian & US GAAP as published in the 1989 Annual Report on Form 20-F, translated at Cdn. \$1.96 to £1 sterling.			
Source:	Exhibit B1			

TABLE 2			
CONSOLIDATED INCOME STATEMENT OF CONSUMERS AND OF BRITISH GAS AND PROFORMA CONSOLIDATED INCOME STATEMENT OF BRITISH GAS REFLECTING THE PURCHASE OF THE CONSUMERS COMMON SHARES			
	British Gas Cdn. \$ (000,000)	Consumers Cdn. \$ (000,000)	Consolidated Totals Cdn. \$ (000,000)
Gas Sales	13,007	1,638	14,645
Gas Costs	<u>7,560</u>	<u>1,216</u>	<u>8,776</u>
Gas Sales Margin	5,447	422	5,869
Transportation of Gas for Customers	<u>-</u>	<u>6</u>	<u>6</u>
Net Gas Distribution Revenue	5,447	428	5,875
Other Revenue	<u>1,776</u>	<u>157</u>	<u>1,933</u>
	<u>7,223</u>	<u>585</u>	<u>7,808</u>
Expenses			
Operation and Maintenance	3,024	210	3,234
Depreciation and Depletion	704	76	780
Municipal and Other Taxes	<u>145</u>	<u>23</u>	<u>168</u>
	<u>3,873</u>	<u>309</u>	<u>4,182</u>
Income Before Financial Charges			
Income taxes & extraordinary items	3,350	276	3,626
Financial Charges			
Interest on Long-Term Debt	390	92	482
Other Interest and Finance Costs	88	27	115
Interest Capitalized	-	(2)	(2)
Interest Receivable	<u>(296)</u>	<u>-</u>	<u>(296)</u>
	<u>182</u>	<u>117</u>	<u>299</u>
Income Before Income Taxes	3,168	159	3,327
Income Taxes			
Current	857	59	916
Deferred	<u>192</u>	<u>(3)</u>	<u>189</u>
	<u>1,049</u>	<u>56</u>	<u>1,105</u>
Net Income	2,119	103	2,222
Minority Interest	6		6
Dividends on Preference Shares	<u>-</u>	<u>(11)</u>	<u>(11)</u>
Income Applicable to Common Shares	<u>2,125</u>	<u>92</u>	<u>2,217</u>
Notes: 1. British Gas - Year to 31.3.89, Consumers - Year to 30.9.89 2. British Gas per Canadian & US GAAP as published in the 1989 Annual Report on Form 20-F, translated at Cdn. \$1.96 to £1 sterling.			
Source: Exhibit B1			

TABLE 3		
COMPARATIVE MOODY'S AND STANDARD & POOR'S BOND RATINGS FOR THE MOST SENIOR RATED DEBT OF THE RESPECTIVE ISSUERS		
Company/Government	Standard & Poor's	Moody's
Government of Canada	AAA	Aaa
Petro-Canada	AAA	Aaa
Province of Ontario	AAA	Aaa
Ontario Hydro	AAA	Aaa
Province of Quebec	AA-	Aa3
Quebec Hydro	AA-	Aa3
Alcan Aluminum	A	A2
Amoco Canada	BBB-	Baa3
BCE Inc.	AA	NR
Bell Canada	AA	Aa2
Canadian Pacific Ltd.	AA	Aa3*
Domtar Inc.	BBB-	Baa3
Gulf Canada Resources	A-	Baa1
Imperial Oil Ltd.	AAA	Aa1
INCO Ltd.	BBB-	Baa2
Interhome Energy	A	NR
Northern Telecom Ltd.	A+	Aa3
The Seagram Company Ltd.	A	A2
Shell Canada	AA	Aa3
TransCanada PipeLines	NR	A3
British Gas plc	AAA	Aaa
* One issue by CP of 9.45% equipment trust certificates due 1988 is rated Aaa. NR Not rated.		
Source: Exhibit E3		

TABLE 4

COMPARATIVE LEVERAGE-RELATED FINANCIAL RATIOS AND VALUE LINE RANKINGS
OF FINANCIAL STRENGTH, SHARE PRICE STABILITY, AND SAFETY

CDN Energy- Related Utility Companies	1989 Total Debt Ratio	1989 Total Interest Coverage Ratio	Financial Strength Rating	Share Price Stability ^a	Price Beta	Safety Rank ^b
NOVA Corp. of Alberta	61	1.66	C++	50	1.00	3
TransAlta Utilities	40	2.16	B++	100	.50	2
TransCanada PipeLines	64	1.80	B+	90	.70	3
Westcoast Energy	56	1.95	B+	95	.70	3
<u>Canadian Energy Companies</u>						
BP Canada	28	1.41	B+	50	.85	3
Bow Valley Ind.	8	5.88	B++	45	.90	3
Cdn. Occidental Petroleum	30	2.55	B+	75	.75	3
Gulf Canada Resources	16	1.91	C++	40	1.10	3
Imperial Oil Ltd.	36	2.49	A+	80	.85	2
Norcen Energy Resources	47	3.77	B	60	.75	3
PanCanadian Petroleum	20	5.79	B+	75	.80	3
Shell Canada Ltd.	21	8.88	A	65	.90	3
British Gas	26^c	7.6	A++	90	.70	1

^a The greatest share price stability is represented by 100, while lower numerical values reflect lesser price stability.

^b Value Line's highest safety rank is 1, while 5 is its lowest rank. The Value Line safety rank is based mainly on each company's relative financial strength and its stock's price stability.

^c Value represents total debt ratio for fiscal year ending 30 March 1989. The corresponding long-term debt ratio for British Gas is 14.5%

Source: Exhibit E3

3. THE TERMS OF THE TRANSACTION

3.1 TAKEOVER BID

- 3.1.1 The Offer will constitute a takeover bid within the meaning of the Ontario Securities Act and will be made by a circular bid prepared in compliance with that act, the regulations thereunder, and other applicable provincial securities laws. The price being offered exceeds certain thresholds, therefore the Offer is not exempt from Part XIX of the Ontario Securities Act and it must be made to all other Ontario holders of Consumers' common shares. The evidence revealed that British Gas intends to extend the same price offer to all minority shareholders regardless of where they reside.

3.2 THE PRICE

- 3.2.1 The Agreement provides that the Offer shall be made in cash at a price for each Consumers common share of \$34

plus

- (a) an amount equal to the difference between (i) dividends for each Consumers common share accruing at the rate of \$0.0052 per day for the period from and including March 2, 1990 to and including the earlier of the date on which Consumers

common shares deposited under the Offer have been taken up and paid for and August 19, 1990, and (ii) the amount of any dividends per Consumers common share declared payable to shareholders of record on a date which falls within such period; and

- (b) interest on \$34 at the rate of 13.2 percent per annum calculated annually for the period from and including August 20, 1990 to and including the date of such take up and payment;

less

- (c) an amount equal to the aggregate of any dividends per Consumers common share payable to shareholders of record on a date which falls within the period from and including August 20, 1990 to and including the date of such take up and payment.

3.2.2 The Agreement further states that the aggregate purchase price may be increased by:

- (a) an amount equal to the proceeds, as determined in accordance with the Agreement, of any sales of Consumers' interest in Arbor prior to the date of the Offer; and
- (b) an amount equal to any proceeds, as determined in accordance with the Agreement, in excess of \$93 million from any sale of Consumers' oil and gas exploration, development and production business prior to the date of the Offer.

3.2.3 The \$34 price per share is about 175 percent of book value and represents a premium of approximately 20 percent over the average of

the closing prices of Consumers common shares on the Toronto Stock Exchange during the 20 trading days preceding March 7, 1990, the date the Offer was publicly announced.

3.2.4 The evidence revealed that the total purchase cost to British Gas will be about \$1.1 billion and that British Gas intends to finance the acquisition initially with short-term debt.

3.2.5 The Board was informed that a committee of the Consumers board of directors, comprised of six directors who are independent of both GW and of Consumers management, was appointed to consider and report to the Consumers board on whether the terms of the Agreement are fair to the minority shareholders of Consumers.

3.2.6 The Directors' circular to the shareholders with respect to the recommendation by the Consumers board of directors, required by securities legislation, need not be sent prior to the date of the Offer.

3.3 DISPOSITION OF ARBOR

3.3.1 Through its wholly-owned subsidiary Congas Holdings Limited, Consumers owns about 90 percent of the common stock of Arbor. Arbor currently owns and/or operates some 4,400 nursing home beds through facilities in Ontario, Florida and Texas. Arbor's business activities are not regulated by the Board.

3.3.2 The 1987 Undertakings specify that, before April 9, 1988, Consumers shall either sell its investment in Arbor or obtain the approval of the Board to continue its investment or participation in Arbor.

3.3.3 Following a hearing in May 1988 to deal with Consumers' request to continue its investment in Arbor, the Board, in its E.B.R.L.G. 30 A/B Decision, allowed Consumers to continue but not increase its

investment in Arbor and did not allow further expansion by Arbor without first obtaining approval of the Board.

3.3.4 In January 1990, Consumers announced its intention to sell its interest in Arbor and the Agreement contemplates that Consumers will sell this interest prior to the date of the Offer. According to the evidence at the hearing, holders of common shares of Consumers may benefit from the disposition of Arbor by an increase in the purchase price to be paid by British Gas in an amount based on the proceeds from such sale. If the sale of all the business carried on by Arbor is not completed prior to the date of the Offer, British Gas will have the option to require such business to be sold to a trust to be established for the benefit of all holders of common shares of Consumers of record on the date of the Offer, in order that such shareholders may still benefit from the disposition of such business following the date of the Offer.

3.3.5 The Board notes, however, that Consumers, in its interim report to the shareholders for the nine months ended June 30, 1990, wrote down its investment in Arbor by \$29 million. According to the interim report this write-down will have no effect on the price to be paid by British Gas.

3.4 POSSIBLE DISPOSITION OF TELESIS

3.4.1 As shown earlier, Telesis, as a Division of Consumers, manages the operations of the following Consumers' subsidiaries:

1. Underwater Gas Developers Limited, a drilling contractor both on and off shore in the Great Lakes;
2. Telesis Petroleums Inc, an oil and gas exploration company, active mainly in the State of Michigan;

3. AOG Investments Limited, a holding company that owns Atlas Oil and Gas Limited; and
4. Atlas Oil and Gas Limited, a company that has a 50 percent interest in four producing gas wells in Alberta which are part of the WGML pool.

3.4.2 In addition, Telesis manages Consumers' leases, gas plants, gas storage and production of gas and oil. The assets of Telesis formed part of Consumers' rate base up to 1986. Since then, the only Telesis asset allowed by the Board in the utility rate base is the cost associated with Crowland storage pool owned and operated by Telesis. All of Telesis' gas production is sold to Consumers, comprising some 4 percent of the latter's gas purchases.

3.4.3 Telesis' gas production comes mainly from Lake Erie with some 25 underwater gas production pools. Total recoverable gas is estimated at about 175 Bcf from these pools, of which about 100 Bcf have already been produced. Consumers' witnesses testified that the larger pools are approaching economic feasibility for gas storage, including a 50 Bcf pool which could be in operation by 1995. They also testified that the advantage of having the activities of Telesis within the utility is that Telesis operates with the long-term objective of finding more gas storage.

3.4.4 The Agreement contemplates that Consumers may sell Telesis prior to the date of the Offer. The possible sale by Consumers of all or part of Telesis arises from a review by Investment Canada which may prohibit the acquisition by non-Canadians of Canadian-controlled financially healthy upstream oil and gas assets. In the event that Telesis is sold for proceeds in excess of \$93 million, holders of common shares of Consumers will benefit from the disposition by an increase in the purchase price to be paid by British Gas.

- 3.4.5 However, British Gas is prepared to purchase Consumers with Telesis intact if the Consumers board of directors chooses not to sell Telesis and if the continued holding of Telesis following the Offer is permitted by Investment Canada. British Gas stated that it will attempt to convince Investment Canada and the Department of Energy, Mines and Resources to allow Consumers to retain those oil and gas reserves with storage potential.

3.5 **EXPIRY DATE OF THE OFFER AND REGULATORY APPROVALS REQUIRED**

- 3.5.1 Either GW or British Gas may terminate the Agreement if the Offer is not made on or before December 31, 1990. In accordance with the Agreement, British Gas will cause the Offeror to make the Offer on or before the tenth business day after the following approvals or requirements, in addition to the LGIC approval, have been satisfied:

- (a) approval pursuant to the Investment Canada Act;
- (b) non-opposition pursuant to the Competition Act (Canada); and
- (c) expiration of the applicable waiting period under the Hart-Scott-Rodino Anti Trust Improvement Act (United States).

Investment Canada Act

- 3.5.2 British Gas is non-Canadian for purposes of the Investment Canada Act and, accordingly, is prohibited from implementing the purchase of Consumers common shares unless that purchase has first been reviewed under that act and the federal Minister of Industry, Science and Technology ("the federal Minister") is satisfied that the purchase "is likely to be of net benefit to Canada".

3.5.3 British Gas filed its application with Investment Canada in June 1990. Based upon its review, Investment Canada will submit a report to the federal Minister. The federal Minister is required by that act, in normal circumstances, to make a determination as to "net benefit to Canada" within 45 days of the date of the application. The federal Minister may extend this time for a further 30 days or for such further period as may be agreed on by British Gas and the federal Minister.

3.5.4 British Gas stated that a determination by the federal Minister will not be made until the decision of the LGIC is known.

Competition Act (Canada)

3.5.5 British Gas is required, under the provisions of the Competition Act (Canada), to give the Director of Investigation and Research Bureau of Competition Policy ("the Director") advance notice of its proposed purchase of the Consumers common shares. This requirement arises solely because the size of Consumers exceeds certain thresholds established in that act. The purpose of the advance notice is to provide the Director with an opportunity to review the relevant details of the purchase and to assess any impact it may have on competition in Canada. The Director has seven days from the filing of the notice to make that assessment, unless he requires further information, in which case he has a further 21 days from the time that further information is filed.

3.5.6 British Gas filed the required notice with the Director on June 26, 1990 and the applicable waiting period has now expired.

Hart-Scott-Rodino Act (United States)

3.5.7 Since Consumers owns some assets in the United States, an advance notice must be given by British Gas in that country pursuant to the

Hart-Scott-Rodino Anti-Trust Improvement Act and a 15 day waiting period must elapse before the purchase of the Consumers common shares can be completed.

- 3.5.8 A notice was given by British Gas in June 1990 and the waiting period has now expired.

3.6 **ASSUMPTION OF SUPPORT AGREEMENTS BY BRITISH GAS**

- 3.6.1 The Agreement further provides that, upon the purchase of Consumers common shares under the Offer, British Gas shall assume, cause to be assumed or otherwise have GW released from:

- a) GW's obligations under certain support agreements dated March 5, 1981 pursuant to which GW is obliged to support the obligations of Consumers in connection with four series of Consumers debentures and the Consumers Preference Shares, Group 1; and
- b) GW's obligations to pay fees calculated on the undrawn portion of four letters of credit dated November 26, 1986 issued by National Bank of Canada as a replacement for the obligations of GW under a terminated support agreement in respect of seven series of Consumers First Mortgage Sinking Fund Bonds.

- 3.6.2 The support agreements were originally entered into by a predecessor of GW in connection with a reorganization of Consumers and certain of its affiliates. Approval for the proposed assumption by British Gas of GW's obligations under the support agreements and letters of credit is specifically required by Article 3.1 of the 1987 Undertakings.

4. POST TRANSACTION

- 4.0.1 This chapter describes the post-transaction structure and financial position of Consumers and British Gas, the plans by British Gas affecting Consumers and the claimed benefits resulting from British Gas owning Consumers.
- 4.1 **OWNERSHIP STRUCTURE AND FINANCIAL POSITION OF CONSUMERS AND BRITISH GAS**
- 4.1.1 As shown earlier and highlighted in the figure on the following page, the final ownership structure is proposed by British Gas to be as follows: Consumers will be owned by Holdco Ltd. which may in turn be owned by Newco Ltd. These are surrogate companies; the actual companies were not incorporated at the time of the hearing. Newco Ltd. will be owned by British Gas International Holdings B.V., incorporated in Holland, which is owned by British Gas Overseas Holdings Ltd., which in turn is owned by British Gas plc. Ownership in each case is 100 percent.
- 4.1.2 As mentioned earlier, British Gas intends to finance its \$1.1 billion acquisition initially with short-term debt.

British Gas plc
(ENGLAND AND WALES)

100%

British Gas
Overseas
Holdings Ltd.
(ENGLAND AND WALES)

100%

British Gas
International
Holdings B.V
(HOLLAND)

100%

Newco Ltd.
(CANADA)

100%

Holdco Ltd.
(CANADA)

100%

The Consumers' Gas
Company Ltd.
(ONTARIO)

Proposed Ownership of
The Consumers' Gas Company Ltd.

- 4.1.3 British Gas' pro forma consolidated balance sheet as at March 31, 1989 and the pro forma consolidated income statement for the year ended at the same date, reflecting the proposed acquisition, have been shown in Tables 1 and 2 respectively. These statements show that British Gas' total assets in the 1989 fiscal year increase by \$2.6 billion to \$29.1 billion. The \$0.5 billion difference between Consumers' \$2.1 billion assets and the \$2.6 billion increase in British Gas' consolidated assets results from the inclusion of the premium shown as "fair value". Income applicable to common shares increases by \$92 million to \$2.2 billion.
- 4.1.4 As can be seen from Table 5 which follows, the acquisition of Consumers with short-term debt will cause the financial position of British Gas to deteriorate somewhat, as measured by generally accepted financial ratio analyses. The common equity ratio, for example, will decline and the total debt ratio will increase by about 10 percentage points. However, as also shown in Table 5, the post-acquisition financial ratios are still superior to those of GW and Consumers.
- 4.1.5 The post-transaction structure of Consumers may change to exclude all or part of Telesis, depending on British Gas' success in convincing Investment Canada and the Department of Energy, Mines and Resources that Consumers should maintain the gas storage related assets of Telesis. The evidence disclosed that exclusion of Telesis in its entirety will have no material impact on the financial position of Consumers.

TABLE 5

RELATIVE RISK OF BRITISH GAS BASED ON FINANCIAL STATEMENT RATIOS					
Financial Ratio	For Fiscal Year^a	British Gas	ProForma British Gas Including Consumers^b	GW	Consumers
Equity Ratio	1989			32.5	32.0
(%)	1988	74.0	64.2	29.9	32.3
Total Debt Ratio	1989			67.5	62.2
(%)	1988	26.0	35.2	70.1	61.4
Times Interest Earned	1989			1.51	2.35
(Before-Tax Basis)	1988	7.63	5.26 ^e	1.53	2.50
Times Interest Earned	1989			1.28	1.87
(After-Tax Basis)	1988	5.43	3.86 ^e	1.24	1.96
Cashflow as % of	1989			6.0	15.1
Total Debt	1988	73.5	48.8 ^e	4.6	15.6
Cashflow as % of	1989			18.6	33.1
Current Liabilities	1988	54.4	43.3 ^e	15.3	30.4
Asset Coverage	1989			1.48	1.61
Ratio (times)	1988	3.77	2.71	1.43	1.63
Net Profit Margin	1989	14.1		2.2	5.7
(%)	1988	14.4	12.8 ^e	1.7	5.6
Return on Average	1989	12.9 ^e		4.2	15.8
Common Equity (%)	1988	19.8	19.7 ^e	3.8	15.4
<p>^a All financial ratios are calculated for the companies' respective fiscal years. "1989" refers to British Gas' fiscal year ending 31 March 1989, GW's fiscal year ending 30 June 1989, and Consumers' fiscal year ending 30 September 1989, while "1988" refers to the previous fiscal year in each case.</p> <p>^b In each year, Consumers' 30 September fiscal year-end results are combined/consolidated with British Gas' results, for the respective year, on a proforma basis.</p> <p>^c Based on historical cost UK GAAP.</p> <p>^e Estimate.</p>					
Source: Exhibit E3					

4.2 PLANS BY BRITISH GAS AFFECTING CONSUMERS

- 4.2.1 Upon completion of the acquisition, British Gas intends that Consumers will continue to operate as a separate and locally managed entity. British Gas, however, stated that it will be in the interest of both companies to have maximum interaction at both the management and operational levels and that this will involve exchanges of information and personnel.
- 4.2.2 British Gas is willing to adopt the 1987 Undertakings which aim to ensure independence of the Consumers board of directors, the continued location of Consumers' head office in the franchise area, the maintenance of an appropriate level of common equity in Consumers' capital structure, and the maintenance of the conditions regarding change of control, and business diversification. British Gas is also ready to incorporate into an undertaking a commitment to use its best efforts to maintain and, where appropriate, increase Consumers research and technology activities. In the event of its re-nationalization, British Gas is prepared to review with the Board additional undertakings to ensure the integrity of the undertakings related to financial matters.
- 4.2.3 British Gas is not inclined, however, to adopt all aspects of the 1987 Undertakings. In particular, it does not believe that the current requirement of having at least a 15 percent public float is necessary. To the extent that this will be a condition of the LGIC, British Gas is willing to re-establish the float only if it can be done without it incurring an economic loss. British Gas sees no need for Consumers' external auditors to be different than those used by British Gas. Further, British Gas requested that Consumers be permitted to participate in a cash management program with British Gas.

4.2.4 With respect to affiliate gas purchase transactions, British Gas is willing to undertake that any gas purchases by Consumers from affiliates be governed by tendering procedures approved by the Board. With respect to affiliate transactions other than gas supply, British Gas is willing to undertake that they be charged for on a basis to be approved by the Board in advance. British Gas proposed that all affiliate transactions be examined on an annual basis by the audit committee of the Consumers board of directors.

4.3 **CLAIMED BENEFITS RESULTING FROM BRITISH GAS' OWNERSHIP**

4.3.1 During the hearing, British Gas testified to a number of benefits which, in its view, will result from its proposed ownership of Consumers and summarized the major ones as follows:

- British Gas is very knowledgeable in the areas of gas distribution, transmission, storage and utilization. As a result, opportunities for operational improvements, synergies and the transfer and exchange of skills will exist to a far greater extent than can be expected with the present owner of Consumers. Moreover, British Gas will be in an excellent position to monitor the performance of Consumers' management and to provide appropriate guidance through its representatives on the board of directors of Consumers.
- British Gas has an impressive record with respect to research and technology which will be available on an open-access basis to Consumers. This can provide opportunities for Canadians to acquire and adapt existing technology, and for Consumers to enhance its research and technology culture.
- The financial strength of British Gas is a positive factor.

- The Canadian economy will benefit from the increase in the capital stock and tax base. Moreover, the proposed acquisition offers benefits in the international trade sense because it confirms the willingness of Canada to participate on a global basis.

5. SUMMARY POSITIONS OF THE PARTIES ON THE PROPOSED TAKEOVER

- 5.0.1 This chapter summarizes the positions of the parties, other than those of the applicants, on the central issue, namely should the proposed takeover be approved.

Consumers

- 5.0.2 Consumers maintained a neutral position.

Union

- 5.0.3 As a major Ontario gas utility, Union claimed a direct interest in the change of ownership issue but did not take an active role at the hearing. In argument, it took the position that, in examining the proposed takeover, the Board ought to apply the same test as it did in its Report to the LGIC, E.B.R.L.G. 34, dealing with the Westcoast/Inter-City takeover transaction. Union maintained that the ownership of a major utility is a public policy issue to be determined by the Government of Ontario; such a policy decision, while it should include the public interest matters examined in this proceeding, encompasses public policy factors which are beyond the scope of this proceeding.

Council of Canadians

- 5.0.4 The Council of Canadians is a national, non-partisan, non-profit organization of some 18,000 Canadians including some 8,000 members in Ontario. Its interest in the takeover arose from its commitment to the preservation and enhancement of Canadian sovereignty in the areas of culture, economics, social and foreign policy and resource development. The Council took an active role at the hearing, urging the Board to recommend against the foreign takeover of a gas utility on the basis that it will seriously compromise domestic economic control of a major public utility which it considers to be integral to the country's oil and gas industry.

Mutual Gas

- 5.0.5 Mutual Gas is a gas supplier to Consumers as agent for industrial, commercial and residential users in the franchise area. Mutual Gas' interest and role at the hearing was limited to issues of protecting the existing deregulated gas supply arrangements. Subject to wishing to extract certain undertakings from British Gas on this issue, it submitted that it has no concerns about the proposed transaction.

The Municipality of Metropolitan Toronto

- 5.0.6 Metropolitan Toronto's claimed interest in the takeover is the future of Consumers employees and the future of the utility as a significant contributor to the local economy. Its role at the hearing was limited to these two issues. It urged the Board to stipulate that certain specified levels of research and development be committed by British Gas as a condition for the takeover of Consumers.

Energy Probe

- 5.0.7 Energy Probe is a public interest group concerned with environmental and energy policy. It is supported by donors, many of whom reside in Ontario. It played an active role at the hearing, particularly in the areas of what is known as least cost planning or integrated resource planning (the provision of energy services at the lowest overall cost, such cost incorporating environmental considerations), affiliate transactions, research and development, and the maintenance of a public float. Energy Probe submitted that the Board should recommend that the proposed takeover be approved if certain additional undertakings are given relating to least cost planning and affiliate transactions and the corporate mission statement of Consumers is amended to include a commitment to energy efficiency and conservation.

F. Warren Hurst

- 5.0.8 Mr. Hurst is a former executive of Consumers. He took an active role at the hearing, including appearing as a witness. He maintained that the takeover should be rejected on the basis that dominant control of a public utility presents incentives for the parent to act contrary to the public interest. He sketched a widely-held ownership scheme (referred to as the ProNational concept) and used it to identify alleged risks to the public interest arising from control of a public utility in general, and from foreign control in particular.

Board Staff

- 5.0.9 Board Staff took the position that, subject to obtaining certain additional undertakings, British Gas has the financial and corporate characteristics, experience and positive intentions concerning Consumers which would allow the LGIC to approve the takeover.

- 5.0.10 Board Staff submitted that Mr. Hurst's wide ownership scheme is an improbable alternative at this time; that Energy Probe's aim to secure from British Gas a serious commitment to the goals of least cost planning and energy conservation is not appropriate for the purpose of this hearing; and that the nature of Consumers' operations makes it unnecessary for British Gas to commit to the undertakings suggested by Mutual Gas.

6. THE ISSUES, BOARD FINDINGS AND RECOMMENDATIONS

6.1 THE ROLE OF THE BOARD AND THE SCOPE OF ITS REVIEW

- 6.1.1 The Board has interpreted its role in this takeover review to be the examination of the effects of change of control of Consumers and its affiliates on the public interest stakeholders, including the consequences for these stakeholders if the transaction were not to proceed.
- 6.1.2 The original concerns which gave rise to the 1987 Undertakings when GW purchased Consumers in 1986, have not altered. The evidence at the hearing indicates to the Board that the undertakings, absent new legislation, are still required.
- 6.1.3 The Board will recommend amendments to specific undertakings which amendments reflect the Board's findings.
- 6.1.4 Appendix B to this Report sets out the Undertakings which the Board recommends should be given by British Gas and its affiliates to the LGIC. The key amendments are underlined.

- 6.1.5 For the purpose of its examination, as required by the Reference, the Board has determined the public interest stakeholders in this transaction to be:
- the gas customers and communities served by Consumers within its franchise areas in Ontario;
 - the shareholders and other investors in the securities of Consumers who reside in Ontario;
 - the Ontario residents employed by Consumers;
 - the Ontario companies and individuals conducting businesses with Consumers;
 - the Government of Ontario, by virtue of its concern with the economic well-being of the province; and
 - the Ontario Energy Board, as the agency responsible for regulating certain activities of Consumers, including the responsibility to fix just and reasonable rates for gas services.
- 6.1.6 These are the same stakeholders as those identified by the Board in its recent E.B.R.L.G. 34 Report dealing with the Westcoast/Inter-City transaction, except for the shareholders of the acquiror company. The Board is of the view that the impact on the shareholders of British Gas does not fall within the scope of its examination.
- 6.1.7 The Board's examination of this transaction has an added dimension, i.e., the acquiror company is not Canadian. The Board is satisfied that, other than limiting the definition of stakeholders, this fact, in itself, does change the basic standards which the Board ought to use in assessing whether the proposed transaction is in the public interest. The Board has interpreted the LGIC's Reference on the foreign ownership question only as a requirement to expand, in some instances, the required analyses and considerations as to the impact of the transaction on the stakeholders.

- 6.1.8 With respect to the notion of the "public interest", the Board reaffirms its view that, rather than attempting to have an explicit definition, it favours a series of tests or measures against which a proposed takeover transaction can be examined.

The Issues

- 6.1.9 The specific matters which the Board considers relevant to the public interest in the proposed transaction are as follows:

- foreign ownership
- the financial strength of British Gas
- the impact of the transaction on Consumers' existing business and financial structure. In particular:
 - a) the maintenance of a public float
 - b) the potential sale of Telesis
- the business plans of British Gas for the utility operations in Ontario. In particular:
 - a) the research and technology activity
 - b) the treasury operations
 - c) affiliate transactions
- the corporate policies of British Gas. In particular:
 - a) the composition of Consumers board of directors
 - b) the Consumers auditors
- undertakings

- 6.1.10 The balance of this chapter presents a discussion of the key issues and the Board's specific findings and recommendations pivotal to the shaping of the Board's overall recommendation on the proposed takeover.

6.2 FOREIGN OWNERSHIP

- 6.2.1 By the terms of the Order-in-Council, the Board was instructed to examine any impact foreign ownership might have on the Consumers' quality of service, the cost of gas to its customers, its level of employment in Ontario and the owner's proposed use of the Consumers' dividends.
- 6.2.2 Some intervenors concentrated all their testimony on this issue, and almost no witness was bereft of some opinion on the subject. British Gas itself was especially sensitive to these concerns and devoted a considerable amount of its direct testimony and its argument solely to this issue.
- 6.2.3 Technical and expert evidence was submitted by several witnesses. Mr. Kierans, called by Board Staff, pointed out the potential benefits, such as technology transfer, and potential negatives, such as the cost associated with servicing foreign investment in Canada through dividends, consulting fees, and so on, but concluded that because Consumers is a regulated utility, the overall impact of foreign control would be neutral to potentially positive.
- 6.2.4 Professor Watkins, also called by Board Staff, and Professor Bradfield called by the Council of Canadians, both maintained that it would be difficult to find any net benefit from foreign ownership for the customers of Consumers or the people of Ontario. Both concluded that without clear undertakings related to research and technology and sourcing, the takeover would impose a cost on Ontario and Canada and should not be permitted.
- 6.2.5 The three expert witnesses called by British Gas - Drs. Reuber, Safarian and Waverman - concluded that on balance, the acquisition

would be beneficial to Canada and Ontario, citing among other benefits, the expansion of Canada's capital and tax base.

- 6.2.6 British Gas submitted that the question of foreign ownership should not be approached on the basis of emotional rhetoric but rather by assessing the merits of any proposed acquisition, having regard to its specific circumstances.
- 6.2.7 British Gas acknowledged the concerns regarding foreign ownership and pointed out that the regulatory regime in Ontario is a form of protection and should provide comfort to those who are concerned with British Gas as a foreign owner. It also indicated that it is willing to enter into appropriate undertakings with the Ontario government to protect the public interest.
- 6.2.8 It pointed out that both the federal and provincial governments encourage appropriate foreign investment and that the purchase, with proper undertakings, of a local gas distribution company like Consumers, was considerably less important to the country's overall economic goals than the foreign purchase of a financially healthy upstream oil or gas producer.
- 6.2.9 British Gas argued that the flow of dividends to an owner resident outside Canada was payment for the benefits accruing to Canada for allowing the foreign investment in the first place and, in any event, payment of dividends to a Canadian owner does not always guarantee reinvestment of those dividends in Canada.
- 6.2.10 However, the company said that: "If there are appropriate investment opportunities in Ontario it is quite likely that British Gas will consider (them) ... and it will be part of Ontario's challenge to create or provide those opportunities."

- 6.2.11 Insofar as a foreign owned company being willing to undertake research in Canada, British Gas pointed to the evidence of Professor Safarian who testified that the studies showed that there was no difference between the amount of research performed by foreign owned companies in Canada and the amount of research being undertaken by comparable Canadian owned companies.
- 6.2.12 Professor Safarian's testimony was also relied upon by British Gas for the contention that the amount of goods imported for use, versus goods imported for direct sale, by a foreign subsidiary are virtually the same as those imported by a comparable Canadian owned company.
- 6.2.13 In order to allay foreign ownership concerns, British Gas undertook to execute additional undertakings to protect Consumers in the event of British Gas being re-nationalized by a future Labour government. British Gas, however, viewed such an event as unlikely.
- 6.2.14 Mr. Hurst, as one of those objecting to the application by British Gas, urged the government not to focus its decision on whether foreign ownership in the abstract was good or bad for Ontario but rather to focus specifically on the appropriateness of foreign ownership of public utilities.
- 6.2.15 He submitted that there was need for a clear government policy in this area because foreign ownership of the province's utilities expanded the "range of uncertainties for the future" and affected the public interest and the enforcement powers of this Board.
- 6.2.16 He argued that it was incorrect and presumptuous of British Gas to conclude that there are no important policy considerations in respect of the foreign ownership of public utilities in Ontario, since in the U.K. there are such considerations as evidenced by the golden share. In his view, Consumers, being the largest gas distributor in Ontario

and Canada, is equally as strategic to our economy and worthy of protection against foreign ownership as British Gas is to its economy.

- 6.2.17 Mr. Hurst expressed concern that, because Consumers would represent such a small proportion of the assets within British Gas and because British Gas has the expressed goal of increasing its profitability by empire building on a global scale, the public interest necessarily embodied in the ownership of Consumers may be sacrificed for some other pursuit in the future.
- 6.2.18 He also noted that British Gas was not prepared to make commitments on matters crucial to the public interest such as the maintenance of a public float or research funding and refused to give even a verbal commitment to support the Ontario economy by undertaking to re-invest any of its dividends in Ontario.
- 6.2.19 Mr. Hurst was critical of the argument by British Gas that there is never a guarantee of dividends being re-invested in Canada no matter who owns the company. In his opinion, if Consumers was widely held in a manner similar to his ProNational concept, the propensity for dividends to stay within Canada would be positive. He maintained that in light of the global ambitions enunciated by British Gas, there is a real likelihood that dividends paid to it by Consumers will not be invested in Canada.
- 6.2.20 Another disadvantage which Mr. Hurst pointed out was the possibility of foreign exchange controls being imposed in the U.K. which could prevent British Gas from fulfilling an undertaking in regard to maintaining an appropriate equity level in Consumers. This concern, he said, could be mitigated by the requirement for a public float.
- 6.2.21 He also submitted that the possibility of a future Labour government re-nationalizing British Gas should not be minimized and that if such

a re-nationalization did occur, the effects on Consumers were not known.

- 6.2.22 Metropolitan Toronto, although it did not lead any evidence, expressed concern in its written argument about the effects of the sale arguing that such a sale promotes the psychology of a branch plant economy which "has fostered a somewhat passive industrial economy in Canada." As well, the Municipality recommended increased commitments by British Gas in the area of research and development.
- 6.2.23 The Council of Canadians made the plea that for practical and philosophical reasons, Consumers, being an integral part of Canada's energy sector, should not be allowed to fall into foreign ownership and control. The underlying concern was fear --- fear of higher rates to customers, fear of loss of research and development, fear of offshore sourcing of supplies, fear of profits being invested outside of Canada, fear that British Gas is more interested in establishing a continental energy market than in serving Canadian interests.
- 6.2.24 The Council of Canadians submitted that Consumers was a critical link in Canada's energy chain and said that great caution should be taken before allowing it to fall under foreign control.
- 6.2.25 The Council was concerned that Consumers' research and development would be reduced; that its staff would be "gutted of talent" to serve the needs of British Gas; that the Company would purchase more of its needs off-shore and that it would be used as a springboard for entry by British Gas into the U.S. market. The Council questioned whether a foreign controlled company would be as concerned about Canada and Canadians as a Canadian owned company would be. These concerns, it said, could not be met by undertakings given to the Ontario government or by regulation of this

Board or by a Canadian presence on the Company's board of directors --- they could only be met by a Canadian owner.

- 6.2.26 Furthermore, in the Council's view, as this Board was not able to oversee the day to day management of the utility, control of the utility by sympathetic owners was critically important.
- 6.2.27 The Council submitted that the financial investment as proposed by British Gas was not as beneficial to Canada as a real investment of an equal amount of money in new facilities and jobs. To justify foreign investment in Canada as an example of open international markets incorrectly equates "maximization of global wealth with the Ontario public interest," it argued.
- 6.2.28 The Council indicated that it was not against a reasonable amount of foreign investment provided that it was real investment, and did not entail giving up control of strategic sectors of the Canadian economy.
- 6.2.29 The best solution, the Council argued, was the transformation of Consumers to a widely held Canadian company.
- 6.2.30 Board Staff submitted that the evidence proffered on this issue was insufficient for the Board to recommend against the transaction on the basis of foreign ownership alone. It argued that the normal process of regulation combined with the proposed undertakings should serve to protect the utility from any potential negative impact caused by the transfer of its ownership to British Gas.
- 6.2.31 Board Staff submitted that the testimony provided by Ms Barlow on behalf of the Council was "in the nature of political commentary" and should therefore be given less weight than the technical evidence presented by others.

- 6.2.32 Board Staff pointed to the evidence that the dollars involved in any potential reduction of research and development in Canada and the possibility of Consumers importing more goods and services, were very small and that other concerns such as location of the head office, independent board of directors and the possibility of re-nationalization were all adequately covered by the proposed undertakings.

Board Findings

- 6.2.33 In the opinion of the Board, the multitude of concerns caused by Canada's branch plant economy as seen by the Council of Canadians cannot be corrected within the confines of an application similar to the one before the Board. The Board's mandate in this case is simply too narrow to encompass the Council's very wide and legitimate concerns about foreign ownership. In any case, none of the more factual, or technical evidence given at the hearing supported Ms Barlow's testimony nor did it support many of the more alarmist conclusions the Council made in its argument.
- 6.2.34 To suggest that Consumers will be "gutted of talent" to serve the needs of its foreign parent or that somehow Consumers will be sacrificed to British Gas' acquisition forays into the U.S. is, at best, hypothetical.
- 6.2.35 The Board agrees with Board Staff that Ms Barlow's testimony should be given less weight.
- 6.2.36 As well, the Board does not find persuasive the argument proposed by some parties that the application should be turned down because Canadians in their turn could not purchase a controlling interest in British Gas. It should be pointed out that the golden share provision serves the same purpose as Section 26 of the Act which requires

government consent to purchase more than 20 percent of the shares of an Ontario utility.

- 6.2.37 British Gas is the only distribution and transmission company in the U.K. and because it also controls a large part of the gas producing fields, its purchase would be similar to purchasing all the local gas distribution companies in Canada, all the gas transmission companies and a high proportion of the gas production companies.
- 6.2.38 The Board is of the opinion that Consumers is not a company which is so vital to the provincial or national economic concern that its ownership, for that reason alone, must remain in Canadian hands. Although its continued operation is important to the economic health of Ontario, the Board's conclusion from examining all the evidence is that, on balance, there would be no profound negative impact on the company or the community if ownership passed to British Gas.
- 6.2.39 Although the question of the concentration of ownership and the need or otherwise of a public float is addressed elsewhere, the Board is of the opinion that its mandate to regulate gas prices within Consumers' franchise area is not diminished solely by the fact that its ultimate owner is a foreign based company. The entity which is subject to the Board's regulation remains Consumers. Its assets, its cash flow, its total income and its entire value remain within this Board's jurisdiction and cannot effectively be removed therefrom.
- 6.2.40 The Board also finds that no significant detriment to the utility or to the community, that cannot properly be protected by adequate undertakings, arises solely as a result of the change to a foreign owner.
- 6.2.41 With respect to the particular issues raised by the LGIC, the Board finds that subject to appropriate undertakings being executed and with

continued regulation by this Board there should be no negative impact on the price of gas or quality of service to Ontario customers resulting from the proposed acquisition.

6.2.42 The Board on the evidence, cannot find that there will be an obvious negative impact on the level of employment by Consumers, although some reorganization may be expected.

6.2.43 The Board cannot predict the extent to which dividends will flow out of Ontario or be re-invested in the Province. However, it notes that some portion of Consumers' earnings would, under ordinary circumstances, be left in the company as retained earnings and be re-invested in plant and equipment. The Board also notes that it does not control the ultimate destination of dividends under the present ownership, not only of Consumers, but also of the other Ontario gas utilities. However, the Board is aware that some portion of the dividends have been invested outside the country, for example the purchase of Arbor.

6.2.44 **Based on all the evidence, the Board finds that ownership and control of Consumers by British Gas, solely because the latter is a foreign company, will not be contrary to the public interest.**

6.3 **FINANCIAL STRENGTH OF BRITISH GAS**

6.3.1 While no party took issue with the financial strength of British Gas, some parties minimized its importance or the relevance of comparing it with the financial strength of GW. They argued that Consumers will continue to face borrowing costs commensurate with its own risk, not British Gas', and financial strength should represent a minimum requirement and not be viewed as an incremental benefit.

Board Findings

- 6.3.2 Clearly a financially strong parent has less need to extract financial resources from the utility to shore up its own financial position and as a result, therefore, the Board places considerable weight on the financial strength of the parent.
- 6.3.3 Based on the evidence at the hearing, the Board finds that British Gas is a financially strong, secure, and flexible entity which can easily finance the purchase of Consumers with additional debt without any perceived risk of impairing its own outstanding international credit ratings or reducing its flexibility to honour its finance-related undertakings. The financial position of British Gas alone or combined with Consumers is indisputably superior to that of GW and Consumers itself.
- 6.3.4 The Board is mindful that neither it nor the Ontario Government has control over British Gas' future business and financial decisions which might seriously affect its financial strength. The Board also takes note that there is a risk, however slight, for British Gas to be re-nationalized under different political circumstances in the U.K., which could adversely change its business and financial structure. The Board considers such concerns, expressed by some parties, to be legitimate. However, it is difficult to speculate what changes might flow from either possibility and to determine, at this stage, the degree to which such events would be adverse to Consumers. To the extent that the proposed undertaking by British Gas relating to re-nationalization may possibly be of some use, the Board accepts British Gas' proposed undertaking to the Government of Ontario with some amendment that, in the event of re-nationalization, British Gas will review with the Board the need for additional undertakings to ensure compliance with the various finance related undertakings already given to the LGIC.

6.3.5 **The Board finds that British Gas is a financially strong company and able to finance its proposed purchase of Consumers. The LGIC should, however, require the undertaking proposed by British Gas that, in the event of re-nationalization, British Gas will review with the Board the need for additional undertakings to ensure continued compliance with the various finance related undertakings.**

6.4 **THE PUBLIC FLOAT**

6.4.1 Currently Consumers is the only Ontario gas utility whose common shares are publicly traded. However, since approximately 83 percent of the shares are presently held by GW-CG, only the remaining approximately 17 percent are actively traded on the Toronto and Montreal stock exchanges. This latter portion of the total outstanding common shares of the Company is known as the public float and the future of these shares was one of the most contested issues in these proceedings.

6.4.2 The market value of the public float consisting of approximately 5.5 million shares, at the price of about \$30 per share at the time of writing this Report, is in the order of \$165 million. At the time of the hearing, these shares were held by approximately 3,500 shareholders.

6.4.3 Article 1.1 of the 1987 Undertaking given by the GW group and Consumers to the LGIC relating the public float reads, in part, as follows:

...no action shall be taken to reduce Consumers' public float of voting common shares below 15 percent of all voting securities without the prior approval of the Ontario Energy Board.

6.4.4 British Gas is required under the Ontario Securities Act, to make its offer to all Consumers' common shareholders in Ontario because the price it is offering provides a premium of more than 15 percent over the average closing value of the shares traded during the twenty days prior to the date the Offer was announced. In fact, the premium is closer to 20 percent. Further, British Gas intends to extend the price offer to all minority shareholders.

6.4.5 The size of the premium ensures that, if the British Gas Offer is made, it will be accepted by virtually all shareholders and the public float will disappear. The issue before the Board therefore is whether or not British Gas should be required to re-establish the float after its purchase of all or virtually all the common shares is completed.

6.4.6 British Gas is prepared to give an undertaking to re-establish on a best-effort basis a public float of at least 15 percent within 10 years of its purchase of Consumers' common shares providing it will incur no economic loss. The proposed undertaking of British Gas in this regard, including its definition of economic loss, reads as follows:

- (a) British Gas plc ("British Gas") will use its best efforts to re-establish a public float of the voting common shares ("Common Shares") of Consumers' in an amount equal to at least 15 percent of the issued common shares. British Gas's obligation hereunder will continue until the earlier of the creation of the 15 percent float and ten years from the date hereof. Nothing herein will require British Gas to re-establish a public float if to do so would result in British Gas suffering an economic loss.

For the purpose of this Undertaking, British Gas would be deemed to suffer an economic loss if the proceeds received by it on a sale of common shares in re-establishing a public float of Consumers' after deduction of all costs associated with such sale would be less than:

- the purchase price in Canadian dollars of such common shares; plus
- a pro rata portion of the costs associated with the acquisition of the common shares of Consumers' by British Gas; plus
- a pro rata portion of the costs of holding the common shares of Consumers' from the date of acquisition until the date of the sale calculated on the basis of the average long term Canada Bond rate over the holding period; less
- all dividends received by British Gas with respect to the shares sold during the holding period or declared during the period and payable to British Gas after such period.

British Gas will make an annual written report to the Ontario Energy Board (the "Board") concerning its efforts to re-establish a public float. In order to expedite the establishment of a public float, British Gas will maintain arrangements with at least two Canadian investment dealers or merchant banks pursuant to which it would sell common shares of Consumers' at any time that such dealer or bank is prepared to purchase such shares for distribution to the public at price which would not result in British Gas suffering an economic loss.

- (b) Until the public float referred to in Article 1.1.(a) is re-established, Consumers' will preserve the continuity of its common share structure, its regular dividend policy, and its per common share and other equity-related performance information (e.g. earnings per share, book value per share and return on average common equity calculations). Consumers' will continue to publish its quarterly financial statements and its annual report in as comprehensive a form as they are currently prepared and these documents will be available to investors and the public in general in Ontario and the rest of Canada through the Globe & Mail and The Financial Post annual report distribution services. In addition, Consumers' will continue to hold a widely publicized and public annual general meeting.

- (c) Subject to Article 3.2, no action shall be taken to reduce the public float created pursuant to subparagraph (a) below 15 percent without the prior approval of the Board.

6.4.7 British Gas emphasized that in the past this Board has never recommended that a gas distribution utility or an owner who acquired control of such a utility, be required to undertake to create a public float. Further, British Gas relied on its financial strength as being sufficient to allow it to contribute equity to the utility without the need to raise new equity funds through a public float. It further argued that, although it recognizes that there are a number of advantages of a public float, none of them is of sufficient benefit to Consumers or the regulator that British Gas should be required to re-establish the public float.

6.4.8 Mr. Hurst, in response to British Gas' argument that since there is no precedent requiring the creation of a public float there is no basis for imposing one, argued that such a position ignores the following crucial considerations:

- it is the action of British Gas in making this offer that results in the elimination of the public float.
- the Board required Article 1.1 of the 1987 Undertakings to ensure that the circumstances now imminent because of the British Gas offer could not occur without Board approval. A requirement for maintenance implies that it is desirable not to eliminate the float.
- Article 1.1 was founded on sound public policy, recognizing the public interest advantages of maintaining a public float.

- 6.4.9 Mr. Hurst submitted that a public float is essential to ensure that the public interest is served and that public utilities and regulatory bodies should strive to achieve a high percentage of public share ownership.
- 6.4.10 He also took issue with the argument of British Gas that access to financial markets for additional equity financing has no value because of the current financial strength of British Gas. He pointed out that, absent a public float, from an equity financing standpoint, Consumers will be completely dependent on British Gas. He argued that since the strategic intent of British Gas is to make further acquisitions, there is no guarantee that its current financial strength will be maintained.
- 6.4.11 Mr. Hurst submitted that a public float provides an indicator through the eyes of the market and the public, of how well Consumers is managed and provides a vehicle to disseminate as much information to the public as possible. He argued that the maintenance of the public float can not only assist the Board but will improve the quality of its final determinations.
- 6.4.12 Mr. Hurst also took the view that one of the benefits of a public float is the ability of Consumers employees to participate in the performance of the utility by purchasing shares and serves as a positive employee incentive.
- 6.4.13 He cited a number of other advantages of maintaining a public float and concluded his argument in this regard, as follows:

...should the Board approve the British Gas ownership, the Company should be required immediately to issue a public float. British Gas has in part engineered the deal which makes a public float "uneconomic" and hence can legitimately be required to absorb these takeover costs. In light of all the prospective uncertainties that may adversely affect the public

interest in the future under British Gas ownership, the maintenance of a public float will provide critical insurance and assistance to the Board in fulfilling its mandate.

- 6.4.14 The Council of Canadians also submitted that a public float would assist the Board in exercising its responsibility in setting the allowable rate of return on common equity. It argued that the ten year period proposed by British Gas was too long and that even after ten years a condition that no economic loss would be incurred virtually makes that condition unenforceable.
- 6.4.15 It further argued that, if the public float was re-established, the Board would be placed in the difficult position of having to consider higher allowable returns to permit the recouping of any economic loss that may result.
- 6.4.16 The Council submitted that the proposal by British Gas regarding the public float is another example of its attitude toward the Ontario public interest, i.e. it takes second place to British Gas' financial interest.
- 6.4.17 Board Staff, through Dr. Cannon, identified the following benefits arising from the existence of a public float:
- the Board's regulation of Consumers is enhanced because independent, market based information is available to the Board to determine Consumers investment riskiness, its appropriate capital structure and cost of equity capital;
 - a public float helps the Board judge fairness and public benefits of non-regulated investments and equity-related affiliate transactions;

- as a result of the public float more information about Consumers is given to the public and the public is therefore more likely to contribute to the regulatory process arising from the increased awareness;
- the public float facilitates raising new common equity capital if the parent could not or would not provide such additional equity funds;
- If a public float existed, Consumers would not depend solely on British Gas' financial circumstances when seeking equity financing, since it will have established a market of its own;
- the issue price of a new share issue would be higher if common shares are already trading in the marketplace;
- the continued responsibility to minority shareholders, many of whom will likely be Ontario residents, is a significant factor in exposing public information about the utility;
- there may be an increase in managerial efficiency by linking executive incentive plans to market performance;
- the availability of stock option plans may enhance employee quality and morale;
- the existence of a public float broadens the range of financing options to include convertible preference shares and convertible debentures;
- low risk, pure utility shares will be attractive to risk-averse, income-oriented Canadian investors which, under the broader public interest, provides an important investment vehicle;
- if a public float of the shares of Consumers were required then some ownership might remain in Ontario, public annual meetings of the company would be held in Ontario and the public would be more likely to maintain confidence in the utility operation where the parent company is a non-Canadian; and

- a 15 percent public float would mean that investment analysts following utility performance would give expert witnesses assistance in analyzing Consumers for rate case purposes.

- 6.4.18 Board Staff argued that the only opposition to the undertaking regarding the public float arises from the private concerns of British Gas about incurring what it described as an economic loss. Board Staff regarded this loss as merely a cost to British Gas of completing the transaction.
- 6.4.19 It submitted that if British Gas' proposal were accepted then it will have achieved indirectly what it cannot achieve directly, i.e. a release from the existing undertaking.
- 6.4.20 Board Staff further submitted that the Board must choose between supporting a public interest goal or accommodating a private interest and urged the Board to recommend in favour of the public interest.
- 6.4.21 It argued that British Gas and GW could have preserved the public float by entering into a different agreement whereby British Gas would offer to purchase only 85 percent of the holdings of each common shareholder, including GW. Such arrangement would have ensured the continuation of the public float.
- 6.4.22 British Gas disagreed with Board Staff's suggestion that the existing undertaking requires a public float and argued that it merely prevents a reduction in the existing public float below 15 percent without Board approval. It further argued that the requirement to create a public float represents a policy change and that the concept was rejected by the Board both in the Unicorp/Union Enterprises (E.B.R.L.G. 28) and Westcoast/Inter-City (E.B.R.L.G. 34) cases.

- 6.4.23 British Gas also disagreed with Board Staff's argument that British Gas and GW could have structured their agreement so that only 85 percent of GW's shares in Consumers would be sold to British Gas. British Gas noted that there was no evidence that this arrangement would have been acceptable to GW, and argued that it is reasonable to assume it would not be acceptable since GW would be absorbing the loss associated with selling its 15 percent remaining holdings to the public at less than \$34 per share. Similarly, the public shareholders whose shares would not be acquired would likely be unable to realize the \$34 price per share.
- 6.4.24 British Gas, noting Mr. Hurst's concern that employees of Consumers will no longer be able to participate in the performance of the utility, pointed out that employees will be able to participate in alternative incentive schemes including a "phantom" share option plan.

Board Findings

- 6.4.25 The Reference requires the Board to report to the LGIC on the maintenance of a public float. As explained in some detail above, there were serious differences of opinion among the parties to these proceedings as to the value or need for the maintenance of a public float either immediately after the transaction is completed or over some specified period of time thereafter.
- 6.4.26 In the Board's view, the need to have a public float can only be resolved by looking at the more general question of what the public interest requires in relation to the circumstances and evidence in this case. In referring to these circumstances, the Board has examined the current undertakings given to the LGIC and the undertakings proposed to be given by British Gas. The two sets of undertakings are substantially different.

6.4.27 In previous cases the Board has made it clear that there are no firm criteria for determining the public interest that will hold true in every situation and, generally speaking, it is preferable not to attempt to define these criteria too closely. The public interest is dynamic, varying from case to case and the criteria by which the public interest is judged by the Board may also change according to the circumstances. In considering the criteria, the Board must use its best judgement as to the particular values of conflicting interests. In this case it must decide whether the public interest would be done any disservice in the event that the British Gas proposal regarding the public float were made a condition of approval by the LGIC.

6.4.28 The Board, in its E.B.R.L.G. 30 Report dated November 17, 1986, at paragraph 3.27, regarding the public float issue, stated the following:

The Board is of the view that it is healthy to have enough public or independent shareholders with interests that may differ from the majority shareholder to achieve the above-noted benefits and also to assist in assuring the Board of Consumers' independence from the interests of the controlling parent and grandparent. It is difficult, however, to set a level which will be appropriate over time and in all circumstances. In the past the Board, although favouring a public float of common shares, has been reluctant to force one. In this case, Consumers' already has a 17 percent public float which, if reduced, could cause the Board some concern.

6.4.29 In that case Gulf was in favour of maintaining a public float of common shares for Consumers because Gulf viewed the public market as a source of equity financing. It also testified that a public float provided flexibility in seeking new financing and is an indicator in the eyes of the market of how well the utility was being managed.

- 6.4.30 The Board notes that much of the debate over this issue dealt with the significance and importance of the public float to the regulator as well as to the utility. However, there was little consideration or discussion as to whether the elimination of the public float would adversely affect the opportunities for Canadians to invest in a major Canadian gas utility. In the Board's opinion this latter consideration must also be given weight by the Board in coming to its judgement.
- 6.4.31 The Board was reminded by some of the parties of its earlier findings in other cases on this issue. In addition to what has already been said concerning the need to look at the circumstances in each case, the Board has reviewed paragraph 9.26 of its E.B.R.L.G. 28 Report to the LGIC in relation to Unicorp and Union Enterprises.
- 6.4.32 The Board regards the Unicorp case as unique. The ownership of a substantial number of the shares in question had already changed hands prior to the completion of the hearing and the Board's Report to the LGIC.
- 6.4.33 In the current case, the Board has held the hearing and will report to the LGIC well in advance of the official offer being made and the share purchase transaction being consummated. In other words, British Gas will be making its Offer with full knowledge of what the rules and/or conditions of approval are going to be.
- 6.4.34 The Board has considered the argument of Board Staff that British Gas and GW could reasonably have arranged to preserve the public float by structuring their agreement so that only 85 percent of the GW held shares would be sold. The evidence in this case is that GW is only interested in selling 100 percent of its holding of the common shares of Consumers. That being so, if British Gas were to acquire only 85 percent of the GW holdings, presumably GW would have to sell its remaining shares elsewhere to its potential disadvantage. In

the Board's opinion, the position taken on this matter in argument by Board Staff is unrealistic.

- 6.4.35 The Board, having carefully reviewed and assessed the evidence and arguments of the parties relating to the advantages and or benefits to the Board as a regulator and to Consumers as a regulated utility, concludes that on balance the elimination of the present public float would not be in the public interest.
- 6.4.36 The Board is also of the view that the residents of Ontario and other Canadians have become accustomed to the opportunity to invest in Consumers' common shares. If the common shares of Canada's largest natural gas distributor were to be removed from public trading, it is the opinion of the Board that that segment of the public interest would be unnecessarily deprived of this opportunity in the future.
- 6.4.37 Further, the Board considers that the employees of Consumers are an important segment of the public interest and that they have, in the past, benefitted from their right to participate in their company's share option plan. If the public float were to disappear, the Board is concerned that current and future employees would be deprived of this meaningful incentive and opportunity to participate in the continued growth of Consumers.
- 6.4.38 Accordingly, the Board finds that the weight of the evidence in this case supports the conclusion that the public float of at least 15 percent of Consumers' common shares should be maintained.
- 6.4.39 With regard to the evidence and argument relating to British Gas' economic loss associated with the re-establishment of this float, the Board notes that there was disagreement among the parties as to the precise definition and calculation of such a loss. Further, British Gas' own witnesses were not in agreement as to whether such loss should

be calculated on a pre-tax or post-tax basis. The Board agrees with the evidence of Dr. Cannon and Messrs. Kierans and Hurst that, whatever the loss or however computed, it should be regarded as an expected cost to British Gas in consummating the proposed acquisition of Consumers' common shares. Clearly, British Gas was fully aware of the current undertaking and one would therefore expect that it could reasonably have assumed that the policy of the Ontario Government and this Board would remain unchanged in this regard. Accordingly, the Board, while recognizing that it is probable that some costs will be incurred upon the re-establishment of a public float, does not accept the British Gas public float proposal. Consequently, there is no need for a finding as to the computation or definition of economic loss.

6.4.40 If all the common shares were to be held by British Gas for a prolonged period of time, there would be some detriment to the public interest. However, the Board finds in fairness that some reasonable period of time should be given to British Gas to re-establish the public float of at least 15 percent of the common shares issued and outstanding. In the Board's opinion, a period of about two years is reasonable. The Board finds, and recommends therefore, that the re-establishment of a public share float shall be completed by the end of Consumers' 1992 fiscal year, i.e. September 30, 1992.

6.4.41 The Board believes that during this two year period, the market place should continue to receive the same type and frequency of information it now receives by reason of the statutory requirements pertaining to companies whose shares are publicly traded. Although British Gas indicated that it was prepared to continue this practice, the Board is of the opinion that it should be formalized into the undertaking dealing with the public float.

6.4.42 **The Board finds that elimination of the public float of Consumers' common shares would be contrary to the public interest and recommends that the public float of at least 15 percent of Consumers' common shares be re-established by British Gas as soon as possible but not later than September 30, 1992. The Board also recommends that an undertaking be given that no action be taken by British Gas or Consumers to alter Consumers' current reporting practices and status as a publicly traded company.**

6.5 **POSSIBLE SALE OF TELESIS**

6.5.1 Telesis is the division of Consumers which, inter alia, leases and operates its Ontario gas production pools which, when exhausted, may become significant gas storage reservoirs. However, federal regulation prohibits the sale of healthy upstream oil and gas producing assets to a foreign owned company.

6.5.2 British Gas argued that it would be desirable but not essential for Consumers to retain its leases over any reservoirs which have storage potential.

6.5.3 Some parties maintained that the public interest is jeopardized with the potential sale or severance of Telesis on the basis that both the gas exploration activity and storage potential in southwestern Ontario would be compromised.

6.5.4 Board Staff went much further and argued that retention of all of the Telesis assets, including its oil and gas exploration arm, was important for Consumers and within the Ontario and Canadian public interest and submitted that a Board recommendation to retain the whole of Telesis would "give a strong indication to Investment Canada that the

position of British Gas in this matter is in the Ontario and Canadian public interest."

Board Findings

6.5.5 The Board finds British Gas' desire to retain within Consumers the leases over gas reservoirs which have storage potential to be well founded but no so important as to become a condition of approval or an undertaking.

6.5.6 There are a number of unknown factors, not least of which is the decision following the review by Investment Canada and the business nature of the potential new owner of these assets. It is not improbable, and perhaps likely, that the assets in question may be eventually owned by an entity whose business interests, and economic justification for acquiring these assets, may be similar to those of Consumers.

6.5.7 The Board finds that the potential sale of Telesis is not a consideration of such significance as to lead the Board to recommend against the British Gas purchase of the Consumers common shares.

6.6 RESEARCH AND TECHNOLOGY

6.6.1 British Gas identified research and development as one of the key areas where benefits would accrue to Consumers as a result of the proposed acquisition.

6.6.2 British Gas invests heavily in research and technology, spending, in 1989, about one percent of its annual sales or about \$150 million on a wide range of research activities including technology for laying mains, electronic gas meters and enhanced efficiencies in gas burners

and appliances. The company is presently constructing a new \$100 million research centre in the U.K. to centralize its research activities.

- 6.6.3 Witnesses for British Gas cited the availability of its extensive technology to Consumers as one of the public interest benefits of its purchasing the Company. Upon completion of the purchase, it was argued that Consumers would have available to it the general know-how and technology of its British parent, some of which is simply not available to other companies even on commercial terms.
- 6.6.4 British Gas also stated that it is prepared to undertake to the LGIC that it will use its best efforts to ensure that research and development undertaken by Consumers is not reduced below current levels and to encourage and support an increase in those activities where this may provide benefits to Consumers and its customers either in the short term or in the long term.
- 6.6.5 In regard to the possibility of British Gas directly commissioning research in Canada, British Gas testified that the company has supported such work in the past and is actively seeking such opportunities at the moment.
- 6.6.6 Mr. Kierans criticized the Canadian gas industry for not devoting more money to research. He testified that the approximately \$1.6 million Consumers spends annually is only about one tenth of one percent of its sales and this, he said, was deficient for an industry that was so important to Canada, and one which he felt was on the edge of a major breakthrough.
- 6.6.7 He was of the opinion that Canada ought to be on the cutting edge of the application of technologies for the extraction, transmission and distribution of natural gas, and suggested an investigation to determine

the reasons for this lack of research and a bold effort to increase what should be valuable exportable technologies.

- 6.6.8 Other witnesses called by Board Staff and by the Council of Canadians testified that there was some evidence that foreign-owned subsidiaries do less research in Canada than Canadian-owned companies. However, testimony of experts called by British Gas indicated that the effect of foreign ownership on Canadian research was neutral or slightly positive.
- 6.6.9 Mr. Hurst, Energy Probe and The Council of Canadians saw nothing but a multitude of problems in the area of research and technology. They pointed out that Consumers had not found it necessary to purchase British Gas technology in the past and they were concerned that it would be very difficult to oversee the fair pricing of technology transfers in the future.
- 6.6.10 They also noted that British Gas had stated that it would not permit competition between it and Consumers when bidding for international consulting jobs as is the case now and that it would stop any research currently being undertaken in Canada which was considered a duplication of research being undertaken in the U.K. They argued that British Gas would appropriate the profits from the development of any technology like natural gas vehicles which Consumers might develop and that Consumers' current policy of looking to Canada first when contracting for research projects would cease.
- 6.6.11 Metropolitan Toronto argued that the Board should recommend approval of the purchase contingent upon British Gas giving a commitment for specified research to be undertaken in the Municipality. It suggested several areas, including natural gas vehicle research and further refinement of a laser currently being used to detect pipeline leaks.

- 6.6.12 Board Staff concluded that there would be no net negative impact in the area of research and technology if the takeover was approved with the undertaking as proposed by British Gas.

Board Findings

- 6.6.13 The Board is of the view that the proposed purchase when completed, will not negatively impact on Consumers' research activities. As to whether there will be positive impacts, the Board notes the comments of Dr. Reuber who said:

...as I understand this transaction, if and when it goes through these two companies will in a sense come together which will provide a series of doors and windows through which technology and all these other benefits can flow more easily than in the present situation. The degree to which that traffic actually goes through those doors and windows will of course depend on the management of both companies, and I can't predict that. Nobody can predict that. ...if we can assume they are reasonable management and we can also assume that they have a considerable incentive to make the most of their opportunities, one can assume then that because of these openings that some traffic will flow and that that will be beneficial to both companies. We can't predict, nor would we pretend to be able to predict, how much that traffic will be.

- 6.6.14 The Board is in no better position to make the prediction that there will be a net benefit to Consumers' research and technology activities if the sale is approved.
- 6.6.15 The Board agrees with those parties who stressed the importance of research and technology and the fact that Canada should have a credible role to play in finding new ways to utilize its vast resources of natural gas.

- 6.6.16 However, the Board does not agree with those intervenors who advocate that undertakings to the LGIC should include the setting of specific research budgets or the assignment of specific areas of research. Such undertakings would be extremely difficult, if not impossible, to monitor and enforce. Furthermore, the Board feels that the public benefits from research and technology are best met when the choice of research projects is driven by product need.
- 6.6.17 The Board is of the opinion that Consumers' current Canadian research expenditures should, at a minimum, be continued and recommends that British Gas enter into an undertaking in that regard as proposed by it.
- 6.6.18 With regard to the Board encouraging an increase in the level of research and technology expenditures and activities, the Board does not feel that the matter was adequately canvassed at this hearing, but consideration of the whole question, and particularly Mr. Kierans' comments, would properly be subjects for the rate cases of all the gas utilities under its jurisdiction.
- 6.6.19 **The Board cannot conclude with any degree of certainty that British Gas' research and technology culture will benefit Consumers. The Board recommends that British Gas undertake to the LGIC that Consumers will maintain or increase its current level of expenditures in the areas of research and technology.**
- 6.7 **TREASURY OPERATIONS**
- 6.7.1 Currently, Consumers' treasury operations are part of a centralized treasury activity at GW, which includes the treasury operations of GW's subsidiaries and those of Olympia & York.

- 6.7.2 According to testimony by some witnesses, the combining of treasury operations results in certain benefits from economies of scale and the ability to attract expert staff. The evidence left the impression that British Gas and Consumers will explore whether there are benefits in combining all or some of the treasury activities and will act accordingly.
- 6.7.3 Certain parties expressed concern that the public interest would not be served if the treasury activity moved away from Ontario.
- 6.7.4 British Gas stated in reply argument that it was considering the merits of establishing a branch of its treasury function in North America which would effectively replicate the activities of GW. However, until such a decision is made, British Gas will make interim arrangements with Consumers or GW to allow an effective treasury function to continue.

Board Findings

- 6.7.5 During the hearing the Board had difficulty ascertaining British Gas' position on the matter of treasury operations. The Board notes that British Gas' final position on this issue does not rule out the possibility that the treasury operations pertaining to Consumers may be conducted from England or elsewhere overseas.
- 6.7.6 The Board accepts that there may be certain tangible benefits associated with the consolidation of the treasury activities between a utility and its parent. The existence of such benefits was the main reason for this Board's past support, subject to appropriate undertakings, in permitting the treasury activities of all three Ontario major gas utilities to be consolidated with their respective parents. The degree to which these benefits may exist may vary from case to

case depending on a number of factors, not least of which is the relative importance of economies of scale.

- 6.7.7 The Board considers that there is an inverse, but not necessarily linear, relationship between utility size and the potential level of benefits arising from combining a utility's treasury operations with those of its affiliates. The benefits to a large utility like Consumers are likely to be relatively less significant than those achieved by a smaller utility. In fact, the Board considers that the size of Consumers and its level of activity in the money markets are such that, if it were to conduct its own treasury operations, any foregone benefits would be marginal.
- 6.7.8 In appraising the likelihood that the treasury operations of Consumers may be conducted from overseas the focus should be on but not necessarily limited to costs.
- 6.7.9 In making such assessment, the Board considers that the treasury function of a utility incorporates a number of important monetary functions, such as short-term borrowing through several financial instruments, issuance of equity and long-term debt, negotiating and managing lines of credit, as well as participating or providing advice on various utility activities, including the planning and budgeting activity and ongoing appearances before credit rating agencies and regulatory tribunals.
- 6.7.10 The Board has difficulty appreciating how some of these activities can be effectively and efficiently orchestrated from overseas. Clearly, any benefits which may exist due to economies of scale are offset by the additional communication costs, the additional risk, and therefore additional cost, involved in operating in different currencies, and the fact that expertise on the Canadian money markets can best be developed in Canada.

- 6.7.11 Moreover, from a broader Ontario public interest point of view, retaining the treasury function within Consumers would result in keeping an important management function in Ontario.
- 6.7.12 Based on all of the evidence, the Board concludes that while there may be some loss of benefits to the Consumers ratepayers if the treasury activity were to stand alone within Consumers compared to the existing situation, the stand alone option, when compared to having such activity conducted from overseas, should be preferred on the basis that it represents the least cost alternative from a ratepayers point of view and from an Ontario broader public interest perspective.
- 6.7.13 Neither the Board nor the other parties at the hearing had an opportunity to canvass British Gas' position, advanced in reply argument, with respect to the planned interim arrangements with GW or the consideration by British Gas of establishing a branch of its treasury operations in North America. The British Gas silence at the hearing about this possibility is inexplicable.
- 6.7.14 The Board has difficulty appreciating the kind of arrangement with GW that is possible, or acceptable, once GW no longer has any interest in Consumers. The Board is not inclined to recommend such an arrangement unless British Gas is in a position to substantiate this proposal with positive considerations which elude the Board at the present time.
- 6.7.15 With respect to the notion of consolidating the treasury operations pertaining to Consumers with a North American branch of British Gas, Toronto being one possible location, the Board views this as a hypothetical situation at this time, not pertaining directly to the matter at hand.

6.7.16 The Board also considers that, in the event British Gas' future business interests in North America may be such that consolidation of the treasury operations may be meritorious, British Gas always has the opportunity to apply to the Board for such consideration.

6.7.17 **The Board recommends that the treasury operations pertaining to Consumers be conducted by Consumers personnel and be located in the franchise area and that this be an undertaking required by the LGIC.**

6.8 **AFFILIATE TRANSACTIONS**

6.8.1 British Gas is willing to accept the existing undertaking relating to affiliate transactions but on balance prefers its own proposals, which are set out below.

6.8.2 With respect to affiliate gas purchase transactions, British Gas proposed that any gas purchases by Consumers from British Gas affiliates be governed by tendering procedures approved by the Board.

6.8.3 With respect to affiliate transactions, other than gas purchases, such as the supply of goods, services or information, British Gas proposed that those transactions be charged for on a basis to be agreed in advance with the Board.

6.8.4 British Gas also proposed that all affiliate transactions be examined on an annual basis by Consumers' external auditors and reviewed by the audit committee of the Consumers board of directors.

6.8.5 On the basis that a "pure" tendering process does not exist, i.e. negotiations still occur on certain gas supply terms and conditions, and that the Board cannot be adequately assured of a competitive price among affiliates, Energy Probe argued for a complete ban on affiliate

gas purchase transactions while Board Staff proposed that they continue to be subject to Board approval.

6.8.6 With respect to affiliate transactions, other than gas purchases, Energy Probe suggested that they should be permitted only if they provide a substantial net benefit to Consumers' customers. Board Staff disagreed with Energy Probe's emphasis on substantial and suggested a modification to the wording of the current undertaking, as proposed by Dr. Cannon, whereby a committee of the independent board of directors of Consumers would be required to review and approve any affiliate transaction before it is reviewed by the Board. With respect to British Gas' pre-approved charge proposal, Board Staff suggested that the Board can deal with this matter in the future on a generic basis to apply to all Ontario gas utilities.

6.8.7 In reply, British Gas suggested that a less burdensome approach to Board Staff's proposal would be for the committee of independent directors of Consumers to review and approve, in advance, the affiliate transactions and report annually to the Board where all parties will have the opportunity to review these transactions at Consumers' rate hearings.

Board Findings

6.8.8 In the Board's view, some of the proposals before it appear to have merit and may be worthy of further consideration. The Board also considers that affiliate transactions are a generic issue affecting all three major gas utilities in Ontario and it is one area where consistency ought to be sought where possible or practical and opportune.

6.8.9 However, the scope of this hearing is to examine the specific takeover proposal. The Board is prepared to consider amendments, changes or

new undertakings which would further the protection of the public interest but it is not prepared to consider changes as significant as those proposed by British Gas, or as dramatic as those proposed by Energy Probe which are not directly related to the acquisition.

6.8.10 **The Board therefore recommends that the existing undertaking pertaining to affiliate transactions be continued without amendments.**

6.9 **BOARD OF DIRECTORS**

6.9.1 In the view of British Gas, the board of directors of Consumers must be comprised of persons who have competence and experience to supervise properly the management of Consumers since competent and experienced directors serve the interest of shareholders and customers alike. Accordingly, British Gas is prepared to accept Article 1.2 of the 1987 Undertakings, that the majority of the Consumers board of directors be independent of British Gas and Consumers and their affiliates.

6.9.2 Although all parties throughout the hearing questioned the degree of independence that could be expected of directors, all of whom would be elected by the majority shareholders, only the Council of Canadians and Mr. Hurst made specific submissions on this issue. The Council of Canadians argued that it would be fair to assume that the interests of British Gas would take precedence over those of Consumers, while Mr. Hurst submitted that it would be unrealistic to suggest that a corporation seeking to acquire total control would do so without the intention of exercising that control through the board of directors.

Board Findings

- 6.9.3 It is recognized that the interests of a corporation may not necessarily always be the same interest as those of the controlling shareholders. However, the common law supplemented by statutory law has done much to ensure that directors of public corporations selected by controlling interests will act in the interest of the corporation.
- 6.9.4 The Board notes that Section 134 of the Ontario Business Corporations Act, 1982 requires every director to: (a) act honestly and in good faith with a view to the best interest of the corporation; and (b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. (emphasis added)
- 6.9.5 The Board also notes that under this legislation, the majority of the directors must be resident Canadian but is of the opinion that, as in the Westcoast/Inter-City case, some percentage should be from the franchise area.
- 6.9.6 In its Report to the LGIC, E.B.R.L.G. 30, the Board dealt with the issue of the independence of the board of directors in some detail and recommended the definition of an independent director which is now incorporated as part of Article 1.2 of the 1987 Undertakings.
- 6.9.7 The Board is of the opinion that this definition of an independent director should be continued.
- 6.9.8 Although no party suggested that some number of directors be appointed by the minority shareholders or some other party, the Board did consider this option but rejected it as minority shareholders have procedural remedies under the legislation to look after their interests and the independence aspect would not be enhanced thereby.

6.9.9 **The Board concludes that with the continuance of the definition of an independent director contained in the 1987 Undertakings, and the statutory requirements related to directors, the independence of Consumers' board of directors will be maintained without additional undertaking requirements, save and except the requirement that one-third of the resident Canadians be from the Consumers' franchise area at the time of their election or appointment.**

6.10 **AUDITORS**

6.10.1 The existing undertaking provides that the auditors for Consumers be different from those of its affiliates. British Gas submitted that this undertaking is neither necessary nor appropriate given the independent nature of auditors. It argued that the presence of different auditors would preclude Consumers from realizing any savings that could be achieved through having the same auditors.

6.10.2 Certain parties questioned the significance of any potential savings and pointed out that, given the foreign ownership issue in this case, having different auditors was of paramount importance.

Board Findings

6.10.3 The Board recognizes that the undertakings governing Ontario's other two major gas utilities do not require that the auditors be different from their respective owners. As pointed out earlier, the Board supports consistency where possible or practical but, at the same time, the Board considers that the differences and idiosyncrasies which may exist from one utility to another, and from one situation to another, should be recognized and not be unduly compromised. It notes that the 1987 Undertakings require separate auditors for Consumers.

6.10.4 With respect to the alleged cost savings, the Board has no evidence before it as to the specific source or magnitude of the potential savings other than general expectations attributable to economies of scale. The Board considers that, if some savings are possible, they can only be minimal. The Board of course must weigh these foregone savings against a number of other public interest considerations.

6.10.5 One of these considerations is that having different auditors for Consumers enhances its independence. As well, Mr. Dodd of GW testified that this requirement has not presented a problem to the present owner. The Board therefore concludes that the reasons which existed in E.B.R.L.G. 30, when the Board recommended different auditors, are still valid.

6.10.6 **The Board recommends that the existing undertaking specifying that Consumers' auditors be different from those of its owners be continued.**

6.11 **CERTAIN OTHER UNDERTAKINGS**

6.11.1 In dealing with the major issues in this chapter the Board has recommended that if the transaction is approved certain undertakings be continued, others be amended and, in certain cases, new ones be added.

6.11.2 The Board also deals with certain other undertakings which either were issues at the hearing or, in the Board's view, require specific comment.

Incorporation/Head Office

6.11.3 The intention of British Gas is that Consumers' head office remain in Toronto and it is prepared to accept the existing undertaking. The

Board concurs with the proposal. Moreover, the Board is of the view that there are certain advantages in respect of enforceability if the parent of Consumers, Holdco Ltd., is incorporated and headquartered in Ontario.

- 6.11.4 **The Board recommends that the direct owner of Consumers be incorporated and headquartered in Ontario.**

Change of Control

- 6.11.5 British Gas is prepared to accept the existing undertaking requiring leave of the LGIC with respect to future changes in control of Consumers but termed unacceptable the requirement to obtain leave of the LGIC in respect of transfers of Consumers to other wholly-owned subsidiaries of British Gas.

- 6.11.6 The Board recognizes that transfers which are entirely within the British Gas structure and which do not alter the ultimate control or financial stability of Consumers may provide certain flexibility to the owners of the utility. The Board, however, considers that this flexibility may result in changes in the ownership structure of the utility which, presumably, the Board may not be made aware of and, most importantly, it will not have had an opportunity to review in respect of public interest considerations. The Board therefore does not recommend acceptance of the proposal by British Gas.

- 6.11.7 **The Board recommends that the existing undertaking pertaining to changes in control continue without amendment.**

Support Arrangements

- 6.11.8 Inherent in approving the proposed takeover is the release of the current owner from its support for certain liabilities of Consumers referred to in Article 3.1 of the existing undertakings.
- 6.11.9 Since British Gas has agreed to replace GW as the guarantor of these liabilities, and given the Board's earlier conclusions and recommendation regarding the financial strength of British Gas, the Board finds that GW should be released from such liabilities upon the assumption of them by British Gas.
- 6.11.10 **The Board recommends that GW be released from the liabilities referred to in Article 3.1 of the 1987 Undertakings and that it be replaced by British Gas.**

Intercorporate Indebtedness, Guarantees and Investments

- 6.11.11 British Gas proposed that the existing undertaking in respect of intercorporate indebtedness, guarantees and investments be amended in order to permit Consumers to participate in a cash management program with British Gas.
- 6.11.12 Consumers suggested that the exception proposed by British Gas be expanded to include routine intercorporate transactions because the undertaking, as it presently reads, places unnecessary restrictions upon Consumers with respect to those transactions involving the subsidiaries and affiliates of Consumers.
- 6.11.13 Elsewhere, the Board recommended that the treasury operations pertaining to the utility to be conducted from its franchise area. The Board views cash management as part of the normal treasury function. The Board is not convinced that any benefits that may arise from

British Gas' proposal, as the Board understands it, will outweigh the costs, at least from the perspective of Consumers.

- 6.11.14 As far as return on investment of surplus funds is concerned, the Board has difficulty seeing how Consumers could be in such a sizeable or sustained cash surplus position to benefit substantially from a joint cash management program with its new owners.
- 6.11.15 On the borrowing side, a joint cash management program may provide Consumers with a nominally lower priced pool of short-term capital but the real cost to the utility will have to include ultimately the costs associated with the risk of foreign exchange exposure and the added communication and administrative costs.
- 6.11.16 For these reasons, and for reasons related to the foreign status of the acquiror as articulated elsewhere in this Report, the Board is not inclined to recommend a joint cash management program with British Gas and its affiliates other than those affiliates which are incorporated and headquartered in Ontario.
- 6.11.17 With respect to the suggestion by Consumers, the Board accepts that intercorporate lending between, for example, Consumers and Gazifère has become a normal finance activity and that this Board has approved a number of applications for such transactions over the years. In the interest of efficiency, the Board is prepared to allow for a mechanism which would partly address Consumers' concerns but at the same time provide this Board with an efficient mechanism in discharging its duties. The Board concludes that application must continue to be made to the Board, however, if no response is received from the Board within 21 business days, the application shall be deemed to have been approved.

- 6.11.18 **The Board recommends that the existing undertaking pertaining to intercorporate indebtedness, guarantees and investments be continued with no amendments other than allowing for a joint cash management program among Consumers and its affiliates which are incorporated in Ontario. The Board further recommends that applications for intercorporate loans shall be deemed to have been approved by this Board if no response is received by the applicant within 21 business days following receipt of the application by the Board.**

Diversification

- 6.11.19 British Gas is willing to accept the existing undertaking that Consumers not engage or invest in any activity that is not subject to regulation by the Board without the prior approval of the Board.
- 6.11.20 Consumers proposed an amendment to the undertaking to preclude a possible interpretation that Consumers may be restricted from even investigating non-regulated investment opportunities without prior Board approval.
- 6.11.21 The legitimacy of Consumers' concern is clear to the Board and it accepts Consumers' proposal.
- 6.11.22 **The Board, therefore, recommends that the existing undertaking pertaining to diversification be amended to allow Consumers to investigate non-regulated investments without prior approval of the Board.**

Enforcement

- 6.11.23 British Gas is ready to submit to the jurisdiction of the Ontario courts regarding enforcement of the undertakings and proposed an undertaking to that effect.
- 6.11.24 The Board concurs with this. However, it notes that British Gas did not oppose the language proposed by Board Staff which was similar but is considered by the Board to be more appropriate. The Board adopts Board Staff's proposal.
- 6.11.25 **The Board recommends that the LGIC require an undertaking whereby British Gas will submit to the jurisdiction of the Ontario courts regarding the enforcement of the undertakings.**
- 6.12 **BOARD RECOMMENDATION ON THE PROPOSED TAKEOVER**
- 6.12.1 Based on the evidence, findings and conclusions in respect of the important issues addressed in this Report, the Board concludes that, on balance, the proposed transaction is not contrary to the public interest if British Gas and its affiliates meet the Conditions contained in Appendix A prior to the formal granting of approval and agree to the Board recommended Undertakings contained in Appendix B.
- 6.12.2 Since the formal granting of approval requires British Gas and its affiliates to produce certain documentation, including the requisite approval pursuant to the Investment Canada Act where the decision by the federal Minister will not be released until the decision of the LGIC is known, the Board recommends that a Conditional Approval be given specifically for the aforementioned purposes.
- 6.12.3 Subject to British Gas and its affiliates fulfilling the Board recommended Conditions and executing the Board recommended

Undertakings, the Board recommends that leave of the LGIC for the change in control of Consumers be granted. In particular,

- leave be formally granted to British Gas in respect of Section 26(2) of the Act;
- leave be formally granted to GW and GW-CG in respect of Article 1.5 of the 1987 undertakings;
- release be formally granted to GW in respect of the support arrangements appearing as Article 3.1 in the 1987 Undertakings and such support arrangements be assumed by British Gas; and
- GW and GW-CG, and their affiliates, be formally released from the 1987 Undertakings.

7. COST AWARDS

7.0.1 Prior to the hearing of evidence in this matter, three of the intervenors applied for funding under the Intervenor Funding Project Act, 1988 and in a written Decision with Reasons dated June 12, 1990 they were awarded the following amounts:

Council of Canadians	\$22,800.00
Energy Probe	\$25,241.80
F. Warren Hurst	\$1.00

7.0.2 By way of a supplementary application Mr. Hurst was awarded \$20,614 by the Board in an oral decision rendered July 3, 1990.

7.0.3 The Intervenor Funding Project Act requires those parties who receive funding awards to account to the Board for their disbursements and any costs awarded at the conclusion of the hearing are to be offset against the award.

7.0.4 At the conclusion of the hearing only the above three parties requested costs.

- 7.0.5 In the June 12 decision, the Funding Panel found that the funding proponents for the awards to Energy Probe and the Council of Canadians were British Gas and GW jointly. Insofar as Mr. Hurst's \$1 award was concerned, the Panel found Consumers to be the proper proponent. In the July 3, 1990 decision, however, in regard to Mr. Hurst's \$20,614 supplementary funding award, the Board held that British Gas and GW should share the expense equally.
- 7.0.6 In his request for a cost award at the conclusion of the hearing, Mr. Hurst argued that Consumers should pay his costs because most of the benefit of his intervention accrued to its customers, employees and investors. He conceded, however, that British Gas and GW had agreed on the record, to jointly reimburse Consumers for any costs awarded against it.
- 7.0.7 Neither of the other two parties seeking costs made any reference as to which party should pay them.
- 7.0.8 In its reply argument, British Gas reiterated its intention to share equally with GW, any costs it is ordered to pay including the Board's costs.
- 7.0.9 The Board, as is its usual practice, hereby assesses the cost awards and the Board's own costs to be paid equally by British Gas and GW.
- 7.1 **Energy Probe**
- 7.1.1 In its argument, Energy Probe requested a cost award of 100 percent of its reasonably incurred costs. It argued that it had no pecuniary interest in the outcome of the proceedings and that its intervention should assist the Board in its determination of the public interest.

7.1.2 For its part, British Gas did not object to Energy Probe recovering some of its costs but in its reply argument, it advocated that 30 percent of the intervenor's reasonably incurred costs would be fair taking into account that:

- about one-half of the testimony given by Energy Probe's witness dealt with least cost planning, "an issue that did not even appear on the issues list";
- its counsels' cross-examination "did not contribute materially to a better understanding of the issues"; and
- given the limited scope of its intervention, any award should include the costs for one counsel only.

7.1.3 On August 9, 1990, seven days after the final date set by the Board for the submission of the applicants' reply argument, Energy Probe's treasurer forwarded further material to the Board, and to the applicants, which it termed, inter alia, its reply argument on the issue of costs.

7.1.4 Other than disagreeing with the British Gas' characterization of its intervention as outlined above, the material summarized the importance of allowing an intervenor's costs and expanded on Energy Probe's request that the Board inform it of any perceived deficiency in its intervention.

Board Finding

7.1.5 The first deficiency the Board finds is that the additional argument in regard to Energy Probe's request for costs was late and should not have been filed at all as there was no provision for reply argument from intervenors, as Energy Probe should have known.

- 7.1.6 The Board points out that if Energy Probe wishes to deal with the Board directly, as it did in this case, it must be deemed to know the rules governing the hearing process and should follow them.
- 7.1.7 The further argument should properly be ignored, but as it does not affect the central issue of this proceeding and British Gas did not see fit to challenge it, the Board will overlook the tardiness of the filing and consider it to be part of Energy Probe's argument proper.
- 7.1.8 Turning to the substance of Energy Probe's request for costs, the Board can only assess the extent of an intervenor's entitlement to costs by measuring the significance of its participation in the process and the value of that intervention to the Board when making its final determination.
- 7.1.9 In that regard, the Board questions the value to this hearing of Energy Probe's emphasis on the subject of least cost planning. Energy Probe did mention least cost planning as one of its concerns in its funding application but the amount of time and effort it devoted to this issue was out of proportion to its importance to the basic issues before the Board.
- 7.1.10 The principles of least cost planning, insofar as they might apply to gas utilities, are not yet fully developed. They are still subject to significant debate and possibly a generic hearing. Energy Probe acknowledged this uncertainty and yet it still advocated undertakings by British Gas to commit to these principles.
- 7.1.11 More than one-third of its argument was devoted to least cost planning and is of marginal use in helping the Board to recommend approval or rejection of the application by British Gas to purchase the shares of Consumers.

7.1.12 Energy Probe's witness also dealt with the subject of affiliate transactions and the Board did derive some assistance from this segment of Energy Probe's evidence and argument.

7.1.13 In the Board's opinion, the remainder of Energy Probe's intervention, focusing on research and technology and the public float, was only of marginal assistance.

7.1.14 At this point it might be helpful to quote from Energy Probe's reply argument, the nature and timing of which was commented upon earlier:

The only question remaining for the Board is the quality of our intervention. Should the Board feel that any part of our presentation was deficient, we would request that you so inform us, that we might correct such deficiency in future interventions. It is not in our interest to provide information that is not helpful, and it is not in the Board's or society's interest to receive such information, but without advising us of which areas were not helpful, should that have been the case, we are likely to inadvertently repeat our errors, to the detriment of all concerned.

7.1.15 The Board trusts that its comments above meet this concern and as a result of the findings herein, the Board will allow 55 percent of Energy Probe's reasonably incurred costs as assessed by the Board's Assessment Officer.

7.2 Council of Canadians

7.2.1 The Council of Canadians also sought 100 percent of its costs for its counsel, consultant and witness but did not seek any amount associated with the appearance of its volunteer president, Ms Barlow. The Council submitted that its intervention was conducted professionally with a view to assisting the Board primarily on the foreign control aspects of the applications.

7.2.2 British Gas argued that the Council should only be awarded 70 percent of its reasonably incurred costs to account for the Board's practice of insuring that an intervenor have an incentive to monitor and control its costs.

Board Finding

7.2.3 The Council of Canadians personified a very important and fundamental issue in these proceedings: foreign control of Canadian corporations. The evidence given by the Council's witness, Professor Bradfield, in combination with the other economic evidence, was helpful to the Board's determination.

7.2.4 However, in the Board's opinion the Council's argument in other areas was less helpful as it tended to overstate the evidence and presented conclusions which were not sustainable by the evidence.

7.2.5 Furthermore the tendency to hyperbolize diminished the effectiveness of the Council's argument thereby lessening the Council's overall assistance to the Board in drafting its recommendations.

7.2.6 The Board awards 60 percent of the Council's reasonably incurred costs as assessed by the Board's Assessment Officer.

7.3 F. Warren Hurst

7.3.1 Mr. Hurst requested 100 percent of his costs. He argued that his intervention was thoroughly prepared and responsibly and thoughtfully advanced. He described his evidence as an able explanation and analysis of a widely-held alternative and its potential for success.

7.3.2 Unlike his initial request for funding, Mr. Hurst did request an amount for costs to cover his personal time or in the alternative, he requested the Board to order a personal honorarium. He also pointed out that the consulting team he employed to assist him did not duplicate each other's efforts but worked separately on different assignments.

7.3.3 British Gas argued that Mr. Hurst should only recover 30 percent of his costs because much of his evidence was irrelevant as it dealt with the ProNational concept and because he should have merged his intervention with other parties to save costs.

7.3.4 As a result, British Gas argued against an honourarium for Mr. Hurst and recommended that the Board closely examine his claims for consultants as none of them testified nor was any of the testimony or argument attributed to them.

Board Findings

7.3.5 In the Board's opinion, Mr. Hurst's intervention was professionally undertaken. The questions put on cross-examination were cogent, precise and helpful to the Board. There was virtually no time wasted and although some of his direct testimony dealt with the ProNational concept, which was not directly an issue, it was nonetheless of assistance.

- 7.3.6 The cursory exploration of the ProNational concept by Mr. Hurst and other witnesses, together with their cross-examination by British Gas and GW was helpful and it allowed the Board to understand more clearly the immense difficulties involved in such an undertaking.
- 7.3.7 As to British Gas' concern about duplication of work amongst Mr. Hurst's consultants, the Board will only permit those costs which, in its opinion were reasonably incurred and not subject to any duplication.
- 7.3.8 The Board has some sympathy with British Gas' position that Mr. Hurst should be responsible for his own personal costs and if he were to be awarded an honourarium, it should be a symbolic amount only.
- 7.3.9 That said, the Board awards Mr. Hurst 75 percent of his reasonably incurred costs, excluding his personal costs, as assessed by the Board's Assessment Officer. The Board further awards an honourarium of \$1,500 to Mr. Hurst in lieu of an award for personal costs.

APPENDIX A

BOARD RECOMMENDED CONDITIONS OF APPROVAL

APPENDIX A

BOARD RECOMMENDED
CONDITIONS FOR THE FORMAL GRANTING OF LEAVE
OF THE LIEUTENANT GOVERNOR IN COUNCIL FOR
THE CHANGE IN CONTROL OF CONSUMERS

The following conditions for the formal granting of leave of the Lieutenant Governor in Council for the change of control of Consumers shall be met prior to the December 31, 1990 closing date set out in the British Gas/GW Agreement.

1. The requisite approval pursuant to the Investment Canada Act shall have been obtained and provided to the Lieutenant Governor in Council.
2. The recommended Undertakings appearing as Appendix B shall be agreed upon and given formally to the Lieutenant Governor in Council to become effective on the closing date of the British Gas/GW Agreement.
3. British Gas and its affiliates shall have submitted a detailed plan, satisfactory to the Lieutenant Governor in Council, to reinstate the public float as described in the Undertakings.
4. British Gas and its affiliates shall have submitted a detailed plan, satisfactory to the Lieutenant Governor in Council, to organize Consumers' treasury operations within Consumers.
5. British Gas and its affiliates shall satisfy the Lieutenant Governor in Council that the immediate parent of Consumers is incorporated and headquartered in Ontario.

APPENDIX B

BOARD RECOMMENDED UNDERTAKINGS

APPENDIX B
BOARD RECOMMENDED
UNDERTAKINGS OF THE CONSUMERS' GAS COMPANY LTD.,
HOLDCO LTD., NEWCO LTD., BRITISH GAS INTERNATIONAL
HOLDINGS B.V., BRITISH GAS OVERSEAS HOLDINGS LTD.
AND BRITISH GAS plc.

TO: The Lieutenant Governor in Council for the Province of Ontario.

WHEREAS GW-CG Investments Limited (formerly 685515 Ontario Inc.) holds approximately 83 percent of the outstanding common shares of The Consumers' Gas Company Ltd. ("Consumers");

AND WHEREAS GW-CG Investments Limited is a wholly-owned subsidiary of GW Utilities Limited;

AND WHEREAS British Gas plc ("British Gas") has entered into a written letter agreement (the "Agreement") dated March 7, 1990 with GW Utilities Limited, for the sale to a subsidiary of British Gas, namely Holdco Ltd. and Newco Ltd., inter alia, of all of the common shares of Consumers held by GW-CG Investments Limited;

AND WHEREAS British Gas has applied to the Lieutenant Governor in Council for leave pursuant to Section 26(2) of the Ontario Energy Board Act, RSO, 1980, c.332 (the "Act") to purchase more than 20 percent of the shares of Consumers;

AND WHEREAS GW Utilities Limited, 706377 Ontario Limited, HWR Holdings Inc., 685515 Ontario Inc. (now GW-CG Investments Limited) and Consumers gave Undertakings to the Lieutenant Governor in Council dated March 4, 1987 relating to, inter alia, the operation and financial stability and control of Consumers and has sought to be relieved from such undertakings if the application by British Gas is granted and the Agreement is concluded;

AND WHEREAS the Ontario Energy Board ("the Board") has held a public hearing with respect to the application by British Gas and has submitted a report and opinion with respect thereto as required by Section 26(2) and 36 of the Act to the Lieutenant Governor in Council recommending that the Lieutenant Governor in Council approve the proposed transaction subject to British Gas and certain related companies satisfying certain conditions and giving certain undertakings;

NOW THEREFORE in consideration of the Lieutenant Governor in Council granting leave to permit the said acquisition, Holdco Ltd., Newco Ltd., British Gas International Holdings B.V., British Gas Overseas Holdings Ltd, British Gas (sometimes collectively referred to as the "Shareholders" and individually as a "Shareholder") as well as Consumers agree to be bound to the following Undertakings to the extent that anyone or all of them can act, refrain from acting or exercise control over the actions of others in order to cause compliance with or to prevent a breach of the said undertakings.

Definitions

"affiliate transaction" shall be defined as purchases and sale of goods, services or information, including gas purchases, or the conferring of a benefit, between the regulated utility portion of Consumers and any associate or affiliate of that regulated portion of Consumers;

"affiliate" shall be defined as in the Business Corporation Act, 1982;

"associate" shall be defined as in paragraph 1(1)4 of the Business Corporations Act, 1982;

"economic dependence" shall be defined as in section 3840 of the Canadian Institute of Chartered Accountants ("CICA") Handbook;

"public float" shall be defined as voting common shares of Consumers not owned or controlled by British Gas or Consumers or any of their affiliates or associates; and

"related parties" shall be defined as in section 3840 of the CICA Handbook.

1.0 Independence of Consumers

1.1 Public Float

- (a) a public float of at least 15 percent shall be re-established by British Gas as soon as possible, but not later than September 30, 1992;
- (b) no action shall be taken by a Shareholder or Consumers to seek permission under the Ontario Securities Act and the Ontario Business Corporation Act, 1982 to alter Consumers' current reporting practices and current status as a publicly traded company; and
- (c) subject to Article 3.2, and following the re-establishment of a public float, no action shall be taken to reduce Consumers' public float of common shares below 15 percent of all voting securities without prior approval of the Board.

1.2 Board of Directors

The majority of the board of directors of Consumers shall be at all times independent of British Gas, Consumers and their affiliates or associates and at least one-third shall be residents in Consumers' franchise area at the time of appointment or election.

An independent director shall exclude, unless the Board otherwise approves, the following persons:

- (a) employees or officers of Consumers or persons retained by Consumers;
- (b) employees, officers and directors of those companies affiliate or associated with Consumers;
- (c) persons in positions of "economic dependence", within the definition provided by the CICA;
- (d) persons who are "related parties", within the definition provided by the CICA; and

- (e) persons who own or control, directly or indirectly, voting shares of Consumers carrying more than 10 percent of the votes attached to all issued and outstanding voting shares of Consumers.

The auditors of Consumers shall file with the Board on the appointment of a new director to the board of directors of Consumers and on an annual basis, (i) with respect to any director who is independent of British Gas, Consumers and their affiliates or associates, a report indicating any related party transactions between or situations of economic dependence in relation to such director and British Gas, Consumers or their affiliates or associates, and (ii) with respect to any director who is not independent of British Gas, Consumers and their affiliates or associates, a report indicating any related party transactions between or situations of economic dependence in relation to such director and Consumers and its affiliates or associates. The auditors shall also confirm that the majority of the board of directors of Consumers is independent within the meaning of the definition set out above.

1.3 Auditors

The auditors of Consumers shall be and shall continue to be different from those of British Gas, its affiliates or associates as long as these entities beneficially own in the aggregate more than 20 percent of the issued and outstanding common shares of Consumers.

1.4 Incorporation/Head Office

The head office of Consumers shall continue to remain in Consumers' franchise area. The entity which directly owns and controls Consumers shall be incorporated and headquartered in the Province of Ontario.

1.5 Change of Control

No action shall be taken by a Shareholder or Consumers, without first obtaining leave of the Lieutenant Governor in Council, that will result in any person acquiring:

- (a) more than 20 percent of the voting shares of Consumers; or
- (b) control of any person that owns or controls, directly or indirectly, more than 20 percent of the voting shares of Consumers where such voting shares of Consumers constitute a "significant asset" of such person.

The voting shares of Consumers shall be deemed to constitute a "significant asset" of a person where the fair market value of the voting shares of Consumers beneficially owned or controlled, directly or indirectly, constitutes 20 percent or more of the aggregate book value of the total assets of such person determined on a consolidated basis in accordance with generally accepted accounting principles.

Application for leave, as required above, shall be made to the Board.

1.6 Treasury Operations

The treasury operations pertaining to Consumers shall be conducted by Consumers' personnel and shall be located in its franchise area.

2.0 Affiliate Transactions

Other than the sale and transportation of gas by Consumers, any affiliate transaction aggregating \$100,000 or more annually and relating to the supply of goods, services or information, including gas purchases, between British Gas and its affiliates or associates, and Consumers shall require prior approval of the Board.

It shall not constitute a violation of this undertaking if Consumers or the associate or affiliate did not know or could have been reasonably expected to know that a transaction was an affiliated transaction.

3.0 Financial Integrity of Consumers

3.1 Support Arrangements

Any support arrangements whereby British Gas will guarantee or support certain bonds, debentures, and preference shares of Consumers presently guaranteed or supported by GW Utilities Limited shall not be altered without the prior approval of the Board.

3.2 Maintenance of Common Equity

There shall be retained in Consumers such portion of the earnings of Consumers as may be appropriate from time to time for retention by a regulated gas distribution utility, and to the extent that at any time such retained earnings of Consumers are not sufficient to maintain the equity of Consumers at the level approved or deemed appropriate by the Board at a public hearing, Consumers shall raise, and/or British Gas and/or its affiliates shall provide, either directly or indirectly, sufficient additional equity capital for that purpose within 90 days (or such longer period as may be directed by the Board), provided that if British Gas and/or its affiliates provide all or part of such additional capital it shall do so on terms no less favourable to Consumers than Consumers could obtain directly in the capital markets.

In the event that British Gas and/or its affiliates intend to provide such additional equity capital to Consumers on the terms referred to above and providing such additional equity capital on the basis then proposed by British Gas and/or its affiliates would result in a breach of Article 1.1(c), British Gas and/or its affiliates shall provide to the Board not less than 30 days notice of its intention to do so and

the effect of providing such equity capital on Consumers public float of voting common shares. British Gas and/or its affiliates shall be entitled to proceed with its intention to provide such additional equity capital after the expiration of such 30 day notice period, notwithstanding that providing such additional equity capital shall contravene Article 1.1(c), unless prior thereto the Board shall instruct British Gas and/or its affiliates not to proceed to provide such additional equity capital because of the potential contravention of Article 1.1(c). In the event that the Board so instructs British Gas and/or its affiliates not to proceed to provide such additional equity capital. British Gas and/or its affiliates shall not have any obligation in that instance under this Article.

3.3 Intercorporate Indebtedness, Guarantees and Investments

Consumers shall not hereafter loan or advance funds to or guarantee or become responsible for the indebtedness or obligations of any person, firm or affiliate, associate or subsidiary of Consumers that is not regulated under the Ontario Energy Board Act, without prior approval of the Board, subject to the exceptions noted below.

Consumers shall not hereafter acquire or pay for securities of any person, firm or affiliate, associate or subsidiary of Consumers that is not regulated under the Act, without the prior approval of the Board, subject to the exceptions noted below.

Exception: This Undertaking does not apply to or include a cash management program with British Gas' subsidiaries which are incorporated and headquartered in Ontario, provided that, if a cash management program is undertaken by any of these British Gas subsidiaries, the subsidiary will provide funds to, or invest cash for Consumers at a cost no higher than that at which Consumers could raise such funds and at rates which are no lower than those Consumers could realize on its own short-term investments.

Exception: With respect to applications relating to intercorporate loans, if no Board response is received by the applicant within 21 business days from the date the application reaches the Board's offices, such application shall be deemed to have been approved by the Board.

4.0 Regulatory Issues

4.1 Acquisition and Reorganization Costs

Consumers shall not include in its rate base or recover in its cost of service any of the acquisition or reorganization costs, including all the costs of employment contracts or arrangements entered into between Consumers and its employees in connection with the acquisition of the shares of Consumers by British Gas or a subsidiary of British Gas.

4.2 Diversification

Subject to the exception noted below, Consumers itself, or through a person it controls, shall not hereafter engage or invest in any activity that is not subject to the regulation of the Board, without the prior approval of the Board.

Exception: This undertaking does not apply to the costs of research, review and preliminary investigation leading to a decision to seek the approval of the Board to engage or invest in any activity that is not subject to the regulation of this Board.

5.0 Re-nationalization of British Gas

In the event of its re-nationalization, British Gas will, if requested to do so by the Board, review with the Board the question of whether additional undertakings are necessary to ensure that British Gas will be able to honour any financial undertakings previously given to the Lieutenant Governor in Council and will enter in such

undertakings as the Board may deem necessary in order to protect the Ontario public interest.

6.0 Research and Technology

British Gas will ensure that research and technology expenditures in Consumers are not reduced below current levels, and will encourage and support an increase in the research and technology activities of Consumers in areas where this may provide benefits to Consumers and/or to the customers of Consumers either in the short-term or in the long-term.

7.0 Public Hearings

Any approval of the Board provided for herein may be granted with or without a public hearing as the Board may determine.

8.0 Status of Undertakings

8.1 Enforcement

The parties hereto agree to be bound by these undertakings.

These undertakings are terms and conditions of the leave granted by the Lieutenant Governor in Council. Any proceeding or proceedings against British Gas to enforce these undertakings may be brought and enforced in the courts of the Province of Ontario and British Gas, its affiliates and associates hereby submit to the jurisdiction of the courts of the Province of Ontario in respect of any such proceeding or proceedings. It is agreed that Consumers is an agent of British Gas, its affiliates and associates for the purpose of service of any process and that personal service of documents on Consumers will be sufficient to constitute personal service on British Gas, its affiliates and associates.

8.2 Past Undertakings

These undertakings supersede, replace and are in substitution for all prior undertakings given to the Lieutenant Governor in Council by GW Utilities Limited, HWR Holdings Inc., 706377 Ontario Limited, 685515 Ontario Inc. and The Consumers' Gas Company Ltd.

Signed and sealed at Toronto this day of , 1990.

BRITISH GAS plc

by: _____

by: _____

BRITISH GAS OVERSEAS HOLDINGS LTD.

by: _____

by: _____

BRITISH GAS INTERNATIONAL HOLDINGS B.V.

by: _____

by: _____

NEWCO LTD. (surrogate)

by: _____

by: _____

HOLDCO LTD. (surrogate)

by: _____

by: _____

THE CONSUMERS' GAS COMPANY LTD.

by: _____

by: _____

